TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1934

No. 374

ROSS C. ADAMS, RECEIVER OF THE FARMERS NATIONAL BANK OF PEKIN, ILLINOIS, PETITIONER,

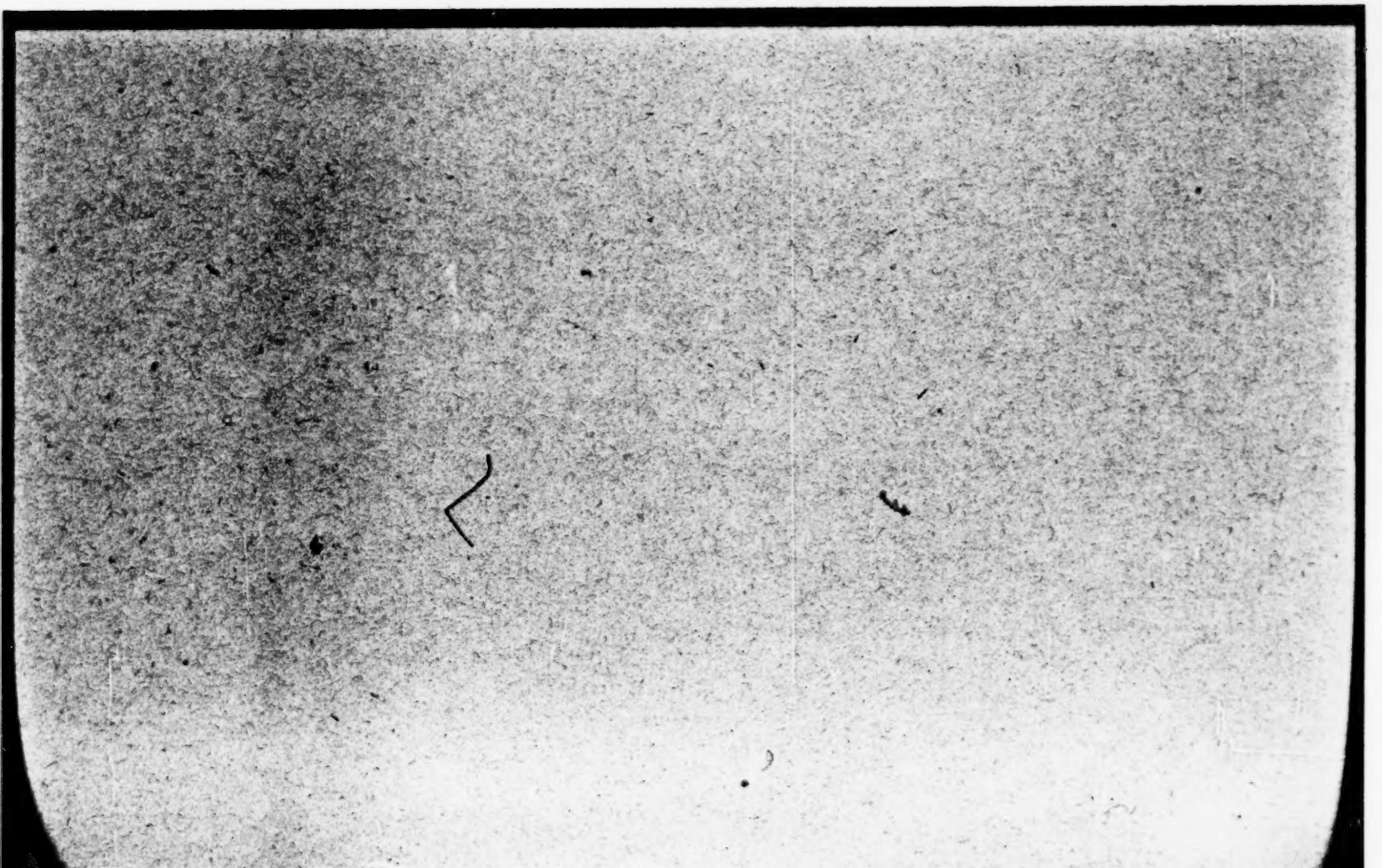
vs.

EDWIN V. CHAMPION, TRUSTEE IN BANKRUPTCY OF JOHN FITZGERALD, BANKRUPT.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

PETITION FOR CERTIORARI FILED SEPTEMBER 12, 1934.

CERTIORARI GRANTED OCTOBER 22, 1934.



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[fols. a-1] [Caption omitted]

[fol. 2]

IN UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF ILLINOIS, NORTHERN DIVISION

Equity. No. 779

EDWIN V. CHAMPION, Trustee in Bankruptcy of John Fitzgerald, Bankrupt, Plaintiff,

vs.

THE FARMERS NATIONAL BANK OF PEKIN, ILLINOIS (a Corporation Organized under the National Banking Laws of the United States of America, Defendant

BILL TO RECOVER PREFERENCES—Filed July 20, 1929

(Caption)

To the Honorable Louis FitzHenry, Judge of said Court:

Edwin V. Champion, a resident of the City of Peoria, County of Peoria, and State of Illinois, in the Southern District of Illinois, Northern Division, and a citizen of the State of Illinois, brings this bill of complaint against The Farmers National Bank of Pekin, Illinois, a Corporation, organized under the National Banking Laws of the United States of America, a resident of the State of Illinois, in the said District and Division, and thereupon complains and says:

I. That this suit in equity brought by the plaintiff, as Trustee in Bankruptcy of John Fitzgerald, under and by [fol. 3] virtue of the provisions of the Bankruptcy Act of 1898, and amendments thereof, in recovery preferences under Section 60-b of said Act.

II. That heretofore, on the 26th day of October, A. D. 1928, and in the District Court of the United States, for the Southern District of Illinois, Northern Division, a petition in involuntary bankruptcy was filed by three (3) creditors against the above named John Fitzgerald, praying that he

be adjudged a bankruptcy, and, thereafter, on the 16th day of November, A. D. 1928, he, the said John Fitzgerald was duly adjudged a bankrupt in said Court.

III. That thereafter, at the First Meeting of the Creditors of such bankrupt, duly called and held before the Refereee in Bankruptcy in charge of such proceeding, the plaintiff herein was duly elected Trustee in Bankruptcy of the Estate of such bankrupt, and that he thereafter qualified as such Trustee and is now acting in that capacity.

IV. That within four (4) months prior to the date of the filing of said involuntary petition in bankruptcy against the said John Fitzgerald, and while the said John Fitzgerald was insolvent and indebted to the defendant, and divers other creditors of the same class, upon unsecured indebtedness provable in bankruptcy, the said John Fitzgerald did within such four months' period, aforesaid, make transfers of portions of his property to the said defendant, as follows:

(a) That, on, to wit, September 1st, 1928, and for a long time prior thereto, the said John Fitzgerald (now bankrupt) was one of the customers and depositors of the said defendant Bank; that on the said 1st day of September, 1928, the said John Fitzgerald had on deposit with the said defendant Bank, subject to check, and credited to his account, a sum equal to or in excess of Fifty Six Hundred and Forty Four Dollars ($5644.00), and that on said day the said defendant Bank took over for its own use and benefit, and absorbed funds so on deposit with said Bank, to the extent of Fifty Six Hundred and Forty Four Dollars ($5644.00), in payment and discharge of debts of the said bankrupt to the said defendant Bank, aggregating the sum of Fifty Six Hundred and Forty Four Dollars ($5644.00), which said debts on the said 1st day of September, 1928, or some one or all of them, were not then due and payable and had not then matured in accordance with the understanding and agreement theretofore had between the said John Fitzgerald (now bankrupt) and the said defendant Bank;

[fol. 4] (b) That, on, to wit, September 6th, 1928, the checking account of the said John Fitzgerald (now bankrupt) with the said defendant Bank became and was over-

drawn in the sum of, to wit, Eight Thousand One Hundred and Seventy Two Dollars and Fifty Cents ($8,172.50); that on said last mentioned date the said defendant Bank demanded of the said John Fitzgerald (now bankrupt) that he, the said John Fitzgerald, secure his said overdraft at said Bank, and that thereatfer, on the said 6th day of September, 1928, the said John Fitzgerald did cause a principal note in the sum of, to wit, Eight Thousand Dollars ($8,000.00), to be given to the said defendant Bank, and the said John Fitzgerald did on the said 6th day of September, 1928, deliver and deposit with the said defendant Bank collaterals belonging to him, the said John Fitzgerald, as security for the said Eight Thousand Dollar ($8,000.00) principal note, and the said John Fitzgerald did also on the said 6th day of September, 1928, pay to the said Bank the further sum of One Hundred Seventy Two Dollars and Fifty Cents ($172.50), which said principal note, for the sum of Eight Thousand Dollars ($8,000.00), secured by collaterals, as aforesaid, together with the said sum of One Hundred and Seventy Two Dollars and Fifty Cents ($172.50), so paid to the said Bank by Fitzgerald, as aforesaid, was received by said defendant Bank in full payment and discharge of the said overdraft of the said John Fitzgerald, amounting to the sum of Eight Thousand One Hundred and Seventy Two Dollars and Fifty Cents ($8,172.50); that the said collateral security so delivered to the said defendant Bank by the said John Fitzgerald on the 6th day of September, 1928, is described as follows:

Eight (8) notes, numbered from 1 to 8, both inclusive, signed by John Fitzgerald, and wife, payable to A. A. Sipfle, Trustee, each for the sum of Five Hundred Dollars ($500.00), dated July 2nd, 1928, due July 1st, 1933, secured by Trust Deed, which is recorded in the Recorder's Office of Tazewell County, Illinois, in Volume 44, at Page 582;

Four (4) notes, signed by the said John Fitzgerald, and wife, payable to Bearer, numbered 21, 23, 24, and 25, each for the principal sum of Five Hundred Dollars ($500.00), dated June 23, 1928, due March 1st, 1933, and secured by Trust Deed by John T. Elliff, Trustee, which is recorded in the Recorder's Office of Tazewell County, Illinois, in Volume 44, at Page 578;

Note of Elmer Veesart to John Fitzgerald, Trustee, num-
[fol. 5] bered 8452, for One Thousand Dollars ($1,000.00), due March 1st, 1933;

That on the following day, September 7th, 1928, the said defendant Bank delivered to the said John Fitzgerald the said Elmer Veesart note for One Thousand Dollars ($1,000.00), and received from the said John Fitzgerald in lieu thereof a note signed by George E. Jenkins, payable to the order of John Fitzgerald, Trustee, numbered 8566, for One Thousand Dollars ($1,000.00), due June 1st, 1933; that said collaterals so received by the said defendant Bank from the said John Fitzgerald (now bankrupt) are of the value of, to wit, Nine Thousand Dollars ($9,000.00);

(c) That, on, to wit, September 7th, 1928, the said John Fitzgerald (now bankrupt) was indebted to the said defendant Bank in the sum of, to wit, Twenty Six Thousand Dollars ($26,000.00), which said debt was evidenced by three (3) promissory notes of the said bankrupt, aggregating the said sum of Twenty Six Thousand Dollars ($26,000.00), all dated April 1st, 1927, which notes from the time of the giving thereof by the said John Fitzgerald (now bankrupt), on the said 1st day of April, 1927, down to the said 7th day of September, 1928, were wholly unsecured; that, on, to wit, September 7th, 1928, the said defendant Bank demanded of the said John Fitzgerald (now bankrupt) security for the said three (3) promissory notes of the said John Fitzgerald, aggregating the said sum of Twenty Six Thousand Dollars ($26,000.00), and, thereupon, the said John Fitzgerald in pursuance of said demand, on, to wit, the 7th day of September, 1928, did turn over and deliver to the said defendant Bank as collateral security for the said notes, aggregating the sum of Twenty Six Thousand Dollars ($26,000.00) property of the said John Fitzgerald, bankrupt, described as follows, to wit:

Note executed by Philip Imig, for the principal sum of Two Thousand Dollars ($2,000.00);

Note executed by V. Meyer, for the principal sum of One Thousand Dollars ($1,000.00);

Note executed by Mary Graff, for the principal sum of One Thousand Dollars ($1,000.00);

Note executed by Charles Graff, for the principal sum of Three Thousand Dollars ($3,000.00);

Note executed by George Z. Barnes, for the principal sum of Five Hundred Dollars ($500.00);

[fol. 6] Nine (9) notes executed by Walter Jones, each for the principal sum of One Thousand Dollars ($1,000.00);

Note executed by Elmer Veesart, in the principal sum of Five Thousand Dollars ($5,000.00);

Note executed by W. C. Sommer, in the principal sum of One Thousand Dollars ($1,000.00);

Note executed by V. Meyer, for the principal sum of Five Hundred Dollars ($500.00);

Ten (10) Shares of Stock, issued by the said defendant Bank;

that the said notes last mentioned were and are of the value of Twenty Three Thousand Dollars ($23,000.00), and the said Bank Stock was and is of the value of Three Thousand Dollars ($3,000.00); that the total value of said property so delivered by the said bankrupt to the said defendant Bank on, to wit, September 7th, 1928, is the sum of Twenty Six Thousand Dollars ($26,000.00), together with accrued interest and dividends thereon; that thereafter (the dates being to the plaintiff unknown), the said defendant Bank collected the said W. C. Sommer note of One Thousand Dollars ($1,000.00), and accrued interest, and the said Charles Graff note of Three Thousand Dollars ($3,000.00), and accrued interest, and has sold and converted into cash said Bank Stock and received therefrom the sum of Three Thousand Dollars ($3,000.00), together with any dividends which were paid on the said Bank Stock from and after, to wit, September 7th, 1928, down to the time of the transfer thereof by the said defendant Bank, and that the said defendant Bank is not now able to return to the said plaintiff said Sommer and Graff notes, and the said ten (10) Shares of Bank Stock, issued by the said defendant Bank.

V. And the Plaintiff avers that the effect of such transfers of the assets of the said John Fitzgerald (now bankrupt) to the said defendant Bank was and is to enable the said defendant Bank to obtain a greater percentage of its debts against the said bankrupt, than any other creditor of the said bankrupt of the same class as the said defendant Bank, and that the said transfers of the said property of the said John Fitzgeral (now bankrupt) to the said defend-

ant Bank did thus operate as preferences of the said defendant Bank under the provisions of the Bankruptcy Act of 1898, and amendments thereto.

VI. That the said defendant Bank received said transfers of assets of the said John Fitzgerald, bankrupt, and each of them, knowing or having reasonable cause to be-
[fol. 7] lieve that it, the said defendant Bank, was receiving a preference under the provisions of the Acts of Congress relating to Bankruptcy.

VII. That the plaintiff, as such Trustee in Bankruptcy, has insufficient assets in his hands to pay in full the debts of the said John Fitzgerald, bankrupt.

In Consideration Whereof, and forasmuch as the plaintiff is without adequate remedy at law,

Wherefore, the plaintiff prays:

1. That the said several transfers of the assets of the said John Fitzgerald, bankrupt, to the said defendant Bank, alleged herein to have been made by the said John Fitzgerald to said defendant Bank, be decreed by this Court to be preferential and in violation of the provisions of the Bankruptcy Act of 1898, and amendments thereof, and that the same be set aside and declared to be wholly void as against the plaintiff.

2. That the said defendant Bank be ordered to account and to return to the plaintiff all of said preferential transfers made by the said John Fitzgerald (now bankrupt) to the said defendant Bank, with interest, as provided by law, and that in case the said defendant Bank fails to return to the plaintiff such assets so transferred by the said John Fitzgerald (now bankrupt) to the said defendant Bank that the said defendant Bank may be required to pay to the plaintiff the value thereof.

3. That the plaintiff may have such other and further relief in the premises as may be just.

4. And May It Please this Honorable Court to issue its subpœna, directed to the said defendant Bank, The Farmers National Bank of Pekin, Illinois (a Corporation, organized under the National Banking Act of the United States of America), commanding it, on a day certain, to appear

and answer this bill of complaint, and to abide by the orders and decrees of the Court thereon.

Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt, by Ira J. Covey, His Solicitor. Ira J. Covey, Solicitor for Plaintiff.

[File endorsement omitted.]

[fol. 8] IN UNITED STATES DISTRICT COURT

REFERENCES TO FILING OF ANSWER, ORDERS OF REFERENCE AND REPORTS OF SPECIAL MASTER

(Caption)

And afterwards, to wit: on the 5th day of November, A. D. 1929, there was filed in the office of the clerk of said court, a certain answer of the defendant to the Bill of Complaint.

(Caption)

And afterwards, to wit: on the 15th day of November, A. D. 1929, there was filed and entered of record in the Office of the clerk of said court, an Order of Reference to Carl Behrman, as Special Master.

(Caption)

And afterwards, to wit: on the 6th day of March, A. D. 1931, there was filed in the office of the clerk of said court, the Report of Special Master Carl Behrman.

(Caption)

And afterwards, to wit: on the 11th day of April, A. D. 1931, there was filed and entered of record in the office of the clerk of said court, an Order of Reference to Carl Behrman as Special Master.

(Caption)

And afterwards, to wit: on the 22nd day of September A. D. 1931, there was filed in the office of the clerk of said court, the Second Report of Special Master in Chancery, Carl Behrman.

[fol. 9] IN UNITED STATES DISTRICT COURT

VIEWS OF THE COURT ON EXCEPTIONS TO MASTER'S REPORT—Filed June 17, 1932

(Caption)

This is a plenary suit by the Trustee in Bankruptcy against the defendant, a national banking association, to recover preferences.

It is charged that within four months prior to the date of the filing of the involuntary petition in bankruptcy against the bankrupt, John Fitzgerald, and while he was insolvent and indebted to the defendant and other creditors of the sale class upon unsecured indebtedness, that he made transfers of portions of his property to the defendant in three different instances, as follows:

(1) The bankrupt was a customer and carried a depositor's checking account with the bank, and, on, to-wit, September 1, 1928, had a balance in his checking account of in the neighborhood of $6,000; that he was indebted to the bank for moneys had and received in the sum of $5,644. The bankrupt had failed to keep his promises to pay the items aggregating the said amount and upon that day the bank appropriated that amount from his checking account to its own use.

(2) On September 6, 1928, the checking account of said bankrupt became and was overdrawn in the sum of, to-wit, $8,172.50; that the defendant called the bankrupt to have executed a promissory note in the sum of $8,000, and on that date procured the bankrupt to deliver and deposit with the defendant collaterals belonging to him as security for said $8,000 note, together with a check for $172.50, which note and check were received by the bank in satisfaction of the overdraft.

(3) On, to-wit, September 7, 1928, the bankrupt was indebted to the defendant in the sum of $26,000, evidenced by three promissory notes aggregating that sum, all dated April 1, 1927, which were wholly unsecured; that on September 7, 1928, the defendant demanded and procured from the bankrupt collaterals as security for the said three promissory notes.

The defendant answered and because the hearing involved the stating of the account between the respective parties, and the large number of criminal cases then pending upon the docket, the cause was referred to a Special Master to take the evidence and report his conclusions and holdings to the Court. Upon the original hearing the Mas-[fol. 10] ter found the issue for the defendant as to the first two claimed preferences and in favor of the plaintiff as to the third, and filed his report in Court. Upon the matter coming into Court, plaintiff took leave to file an amendment to his bill; the answer was extended to the bill as amended and the cause rereferred to the Special Master.

The amendment to the bill changed the character of the first two of the three original causes of action. As to the first:

1. It was charged that the sum of $5,644, appropriated from the bankrupt's checking account by the bank in satisfaction of indebtedness due the bank, was a part of the sum of $36,350, deposited with the bank on August 30, 1928, for the purpose of paying off certain bonds which were a lien upon a farm formerly owned by the bankrupt and which, on the day previous, the bankrupt had transferred to a purchaser, with the express understanding and agreement that the sum of $36,350, received by the bankrupt from the purchaser would be used to pay off certain bonds, which facts were well known to the defendant and its officers; that the fund was not of the character of deposit to which the bankers' common law lien attaches, was not made in the usual course of business of the bankrut for general purposes, but was impressed with a special purpose.

2. The amendment to the bill affecting the second cause of action was probably suggested to the pleader by the holding the of the United States Supreme Court in Dean v. Davis, 242 U. S. 438, 37 S. C. R. 130, where it was held in that particular case, that the proof did not show a voidable preference under Section 60 of the Bankruptcy Act (¶96, Title 11, U. S. C. A.), but did show a fraudulent conveyance or transfer under Section 67 (e) (¶107, Title 11, U. S. C. A.). It charges that the defendant had received for collection from correspondents the bankrupt's $2,000 check, dated, to-wit, August 31, 1928, payable to Sophia K. Hindahl, and a check dated, towit, September 1, 1928, pay-

able to E. C. Robison, and drawn on the defendant for $6,172.50, both of which checks were in payment of previous existing debts. Upon receipt of these checks the bankrupt was notified there was not sufficient funds in the bank to his credit to pay the checks, or either of them; that the bank would protest them; that upon the same day the defendant procured the son-in-law of the bankrupt, George Barnes of Peoria, to come to Pekin; upon his arrival at Pekin, Barnes executed to the bank his personal note for [fol. 11] $8,000, which was secured by notes or bonds of the value of $9,000, belonging to the bankrupt; that the bankrupt gave to his attorney his check for $172.50, which together with the amount procured upon Barnes' note for $8,000 would be sufficient to pay the two checks. The bank issued its certificate of deposit to Barnes for $8,000, which was endorsed by Attorney Black; Attorney Black endorsed the said certificate of deposit and deposited it together with the bankrupt's check for $172.50 in his account with the defendant, and thereupon drew his personal check on the bank for $8,172.50, which was paid; thereupon the bank forwarded through its correspondents, the collection of the Hindahl and Robison checks. The amendment further alleged that the transfer of the securities to the bank and the payment of the checks received by the defendant for collection was a fraudulent transfer.

The amendment did not change the third cause of action.

Upon the coming in of the second report of the Special Master, he adhered to his former holding in favor of the defendant on the first and second causes of action. In due time *due time* the plaintiff filed exceptions as to the findings and holding of the Special Master as to the first two causes of action, and, the defendant filed exceptions to the findings and holdings of the Special Master as to the third cause of action; that is, the procuring of collaterals to secure the bankrupt's straight promissory note.

The findings and holdings of the Special Master as to the first cause of action were admittedly correct.

The findings and holdings as to the second cause of action are very seriously attacked by plaintiff. Running all through the evidence in this case are expressions of fear of an approaching visit by a National Bank Examiner from the office of the Comptroller of the Currency. The bankrupt was a stockholder and director of the defendant bank

and Chairman of the Committee on Loans and Discounts of the Board. In 1920 he had reached his limit as a borrower from the bank of ten percentum of the amount of the capital stock and unimpaired surplus of the bank, which was $26,000. At that time and until probably 1927, straight promissory notes executed by him would have been regarded as gilt edged. He was not only a large land owner, but had a very large loan business and was constantly dealing in real estate transactions, financing the deals for his customers; he was a loan agent in Pekin and Tazewell [fol. 12] County for one of the large old line life insurance companies. The deflation of agriculture in 1920, of course, had its effect upon him. In his latter years he was negligent in the transaction of his business, refinanced large loans, placing new mortgages upon property to pay off the old ones, and neglecting to file the releases of the first mortgages, and, to cancel the notes secured by them, so that there were outstanding duplicate mortgages upon the same property and duplicate sets of notes secured thereby. His standing in the community was so unquestioned that clients who had money to loan would give it to him with instructions to invest it and he would give such persons receipts therefor and use the money as his own, and, presumably, pay his clients' interest thereon. So, during the years before his bankruptcy he was constantly engaged in financial transactions and necessarily the holder of many notes secured by mortgages.

The defendant bank's officers, at the various almost daily meetings of the bank's Committeee on Loans and Discounts, were intimating and suggesting that he give the bank collateral security for his $26,000 personal notes. He needed money, but the bank and the bank officers were careful not to permit his name to go upon any additional obligations, so that it became necessary for him to use the names of other persons, including his son and son-in-law, furnishing collateral security for any sums in the names of other persons. This was apparently for the purpose of hiding his operations from the bank examiner. He had been required to put mortgages on his unencumbered lands in Tazewell County in May of 1928. His stock of collaterals was getting low and it was becoming inconvenient for him to meet his legitimate obligations. This was the situation that existed on September 6, 1928, when the bank received,

through its correspondents, the two checks aggregating $8,172.50, for collection.

Less than a week before, the President of the bank found it necessary to assert the bank's common law lien and charge to his open checking account the sum of $5,644, for which he had repeatedly promised he would give the bank checks, but did not do so. The President of the bank, Mr. Sipfle, had reached the conclusion that the bank would permit the bankrupt to overdraw his checking account no further. The bankrupt's balance in the bank was very small. It is apparent from the record that he feared what the bank examiner might say if he loaned the bankrupt sufficient sum- to meet the checks, even though Fitzgerald [fol. 13] would deposit an ample amount of collaterals to secure the money. So, the bankrupt Fitzgerald, and Sipfle, the president of the bank, had the bankrupt's son-in-law, Mr. Barnes of Peoria, come to Pekin. A device was resorted to. Mr. Sipfle had concluded to loan the son-in-law a sufficient sum to pay the aggregate of the checks, provided ample collateral security should be deposited. With this object in view, Barnes gave his personal note to the bank for $8,000 and deposited $9,000 worth of collaterals as security, which collaterals were furnished by Fitzgerald.

The bank issued its certificate of deposit for $8,000 to Barnes, who endorsed it to Judge Black, then the counsel for Fitzgerald, and the latter's check for $172.50, deposited them to his own account and gave the bank his check for a sufficient amount to pay the two checks aggregating $8,172.50, which had been received for collection. The evidence shows, immediately upon the payment of the amounts of the checks to the bank, it remitted to the sending banks the amounts of the respective checks sent it for collection.

When carefully considered, it will be observed that the transactions of September 6th involved two separate matters: (1) The receipt for collection of the two checks and the remittance of the proceeds; and (2) the creation of the fund for the payment of the checks. The payees of the checks are not parties to this suit. What the judgment of the Court might be if they were, is a matter now unnecessary to discuss, but the chief question involved is whether or not under this second charge the Trustee may recover the value of the securities furnished by the bankrupt as security for the note given by Barnes.

Assuming that the Barnes note was in fact that of Fitzgerald and the effect of it was the making of an excess loan to the bankrupt, in violation of Section 84, Title 12, U. S. C. A., that fact would invalidate the transaction although it might make the officers of the bank subject to a penalty.

Insofar as the bank was a party to the creation of the fund out of which the Hindahl and Robison checks were paid, the bank was not a creditor and gave a fair present consideration for the collaterals give- to it to secure the payment of the note.

The Master correctly found that no preference was effected so far as the defendant bank was concerned, under Section 60 (b) of the Bankruptcy Act. Dean v. Davis, supra. Nor was the transaction a fraudulent conveyance [fol. 14] or transfer within the meaning of Section 67 (e).

In this case it must be borne in mind that the owners of the checks, who were the only creditors involved in the transaction—Hindahl and Robison—had nothing to do with the raising of the fund and knew nothing about it, so far as the record in this case shows. The defendant bank was the agent of the owners of the checks to collect and remit only. The record shows that immediately after the checks were collected, the proceeds were remitted to the forwarding banks. With notice to the defendant bank of the manner in which the fund was created upon the remittance of the proceeds, within the rule that money paid to an agent and lawfully accepted, may not thereafter be reclaimed by one who has made the payment with notice of the agency, if before the attempted reclamation the agent in good faith has settled with the principal. Carson v. Federal Reserve Bank, 254 N. Y. 218; 172 N. E. 457, A.L.R. Vol 7, p. 435.

The recovery here under Section 67 (e) is sought upon the authority of Dean v. Davis, supra, and other cases. In Dean v. Davis, supra, the Trustee in Bankruptcy sought to recover a property of the bankruptcy estate under Section 60 (b), and also Section 67 (e) of the Bankruptcy Act. The Court held that under the facts in that case there was no preferential transfer under Section 60 (b), but permitted a recovery under Section 67 (e), which provides that if a debtor, within four months before the filing of the petition in bankruptcy, makes any transfer with the intent and purpose on his part to hinder, delay, or defraud his creditors, or any of them, it shall be null and void, except as to pur-

chasers in good faith and for a present fair consideration, and that it shall be the duty of the Trustee to recover the same.

In that case Jones was a farmer and owner of a country store. A bank having discounted his notes bearing endorsements which it later concluded had been forged, demanded that Jones take up the notes. Fearing arrest, he appealed through his father to his brother-in-law, Dean, for a loan of $1600, promising to secure it by a mortgage on all his property, which he represented was worth more than five times the amount. Dean provided the money and on September 3, 1909, acting in conjunction with Jones' father, "took up" the notes. Most of them were not yet due. A mortgage deed of trust, dated September 3, 1909, was executed September 10 and recorded September 11. It covered practically all of Jones' property, including the stock [fol. 15] in trade, accounts, store, furnishings and fixtures, household furniture and goods, live stock, crops standing and cut, and the farm itself, the last subject to a prior deed of trust. Four mortgage notes were given, payable respectively in seven, thirty, sixty and ninety days, with a proviso that upon default of any one, all should become payable. The first note—and hence all—was overdue when the mortgage was recorded. On that day, Dean directed that possession of the property be taken, which was done on September 13th (the 12th being Sunday). Jones was at that time deeply insolvent and had many unsecured creditors. Some of these immediately challenged the validity of the mortgage. Within a few days an involuntary petition in bankruptcy was filed and Jones was adjudicated a bankrupt. The mortgaged property was converted into cash and under an agreement with general creditors that it should be deposited to await the ultimate determination of the rights of the parties, it yielded $1634, leaving nothing for the general creditors if the mortgage was held valid.

The case of Dean v. Davis, supra, had been tried by the District Court, which found the transfer by Jones to Dean was a fraudulent conveyance within the description of Section 67 (e) and that it was executed with the intent and purpose on Jones' part to hinder, delay and defraud his creditors. Dean appealed to the Circuit Court of Appeals, where the decree of the District Court was affirmed and the case appealed to the Supreme Court. Dean was in full posses-

sion of all of the facts, took a mortgage upon all of Jones' property, which Jones claimed was worth five times more than the amount of the debt. The Supreme Court, in the opinion in the Dean case, in discussing liability under Section 67 (e) said:

"Jones knew that he was insolvent. He knew that he was making a preferential payment. He must have known that suspension of his business and bankruptcy would result from giving and recording a mortgage of all of his property to secure a note which had matured before the mortgage was executed. The lower courts were justified in concluding that he intended the necessary consequences of his act; that he willingly sacrificed his property and his other creditors to avert a threatened criminal prosecution; and that Dean, who, knowing the facts, cooperated in the bankrupt's fraudulent purpose, lacked the saving good faith."

[fol. 16] In the instant case the creditors were Hindahl and Robison; they knew nothing about how the fund was created, had no part in it, had only deposited the checks to their respective accounts with their local banks, which transmitted them to the defendant for collection.

The Trustee relies very strongly upon the cases of In re Beerman, 112 Fed. 663, and Wallers v. Zimmerman, 208 Fed. 62, to sustain a recovery and especially urges those cases upon our consideration, because they were cited by the Supreme Court in Dean v. Davis, supra. However, they were cited upon a different proposition. They were cited as an illustration of the principle, "but a transfer to a third person is invalid under this section as a preference only where that person was acting on behalf of the creditor * * *." Here, Dean acted in the debtor's behalf in providing the money and taking up the notes.

The record is wholly silent upon the facts concerning the issuing of the Hindahl and Robison checks. The presumption is that they were issued in the regular course of business by the bankrupt, and received and cashed in regular course.

In Lowell v. Merchants National Bank, 283 Fed. 124, a case somewhat similar to the present one, the Court said:

"No case has been called to the attention of the Court holding that a bank is liable under the Bankruptcy Law to

refund money paid out on a depositor's checks, even though the check is given a creditor for the purpose of preferring him. Nothing short of active fraud or collusion on the part of the bank with the preferred creditor could furnish the foundation for the maintenance of such a claim. (Rubenstein v. Lottow, 220 Mass. 156)."

It is true there was a circuitous performance in connection with creating the fund with which to pay the bankrupt's two checks in question, but this was done for the purpose of preventing the name of the bankrupt from appearing on any more paper due the bank in any sort of transaction which might thereby create criticism on the part of the National Bank Examiner, whose visit was apparently impending.

The Special Master found the equities in favor of the defendant on the second cause of action, and we feel from a careful examination of the record that he was warranted in so doing.

The third cause of action is one to recover the $26,000 worth of collaterals or the proceeds of any which had been collected by the bank and which were procured, accord-[fol. 17] ing to the testimony of the president of the bank, on September 7, 1928, the day following the happenings of the events involved in the second cause of action. The merits of this controversy depend entirely upon the findings of fact and involve two propositions:

1. Did the defendant have reasonable cause to believe that on the 7th of September, 1928, the bankrupt, John Fitzgerald, was insolvent and that the procuring of the collaterals on that date would enable the defendant to procure a larger percentage of its indebtedness due from Fitzgerald than other creditors of the same class? And,

2. Did the bank have any collaterals in its possession, procured by it from John Fitzgerald in June and July, 1928, as security on his straight promissory notes aggregating $26,000?

And examination of the record and the Master's first report shows that the Master gave the third cause of action meticulous consideration. Counsel for the bank on the hearing upon exceptions to the Master's report and in his written brief complains bitterly because the Master had accorded the bankrupt entirely too much credibility as a wit-

ness. Fitzgerald, the bankrupt, had been indicted for criminal practices in connection with his loan business; he had pleaded guilty, was sentenced to the penitentiary, was finally paroled, and died. While in the penitentiary he was called as a witness and testified in the case. He was uncertain about the date when the collaterals were procured by the president of the bank and could not state positively whether it was the 7th or the 17th of September. The date is fixed certainly by the president of the bank as the 7th, because that was the date the collateral records of the bank show there were $26,000 worth of collaterals held by the bank as security for John Fitzgerald's $26,000 notes.

Early in September there was considerable talk between Fitzgerald and Sipfle, the president of the bank, and the other members of the Loan and Discount Committee of the bank. Fitzgerald explained that the Examiner had examined the bank and was ready to leave, but that Mr. Sipfle came to his office and said the Bank Examiner refused to leave until this matter was taken care of. Whereupon the securities and bank stock in question were delivered to Sipfle. There is nothing in the record that shows just when the Bank Examiner did come to Pekin, or when he left, but that fact is not material.

[fol. 18] John Fitzgerald, in his lifetime and prior to his bankruptcy, was one of the leading citizens of Pekin. He was a large land owner and did a large loan business. Mr. Sipfle became president of the bank in 1919, accepting the office only upon the condition that John Fitzgerald would assume the chairmanship of the Loan and Discount Committee. Fitzgerald, Sipfle and Reiss, the vice-president, constituted the committee, they met daily throughout the years. A very large portion of the bank's business involved agricultural paper and farmers'. When Fitzgerald became chairman of the committee, he was regarded as a wealthy man. Throughout the entire period he was also the local agent for one of the old line life insurance companies. They all undoubtedly knew that with the deflation of agriculture in 1920, farm values and farm loans shrank in market value steadily, and this process continued up until Fitzgerald's bankruptcy.

Fitzgerald was one of the largest customers of the bank; all of his insurance company's loan business as well as his

individual business was done through this bank. At one time his insurance loan business amounted to considerably more than $2,000,000, and at the time of his failure although it had shrunken some it was still quite substantial, being considerably over $1,000,000. Mr. Mott, the cashier of the bank, was quite conversant with all of Fitzgerald's loans and paper. Judge Black was Fitzgerald's attorney, except that upon one or two occasions he did represent the bank in small matters, but did not become attorney for the bank until after Fitzgerald's failure.

In 1920, Fitzgerald had reached the maximum of his borrowing power under the law from this bank, the limit was $26,000. Throughout the years his note was undoubtedly regarded as good. During the last year, 1928, his associates began pressing him for collateral security. He always promised the other members of the committee that he would fix the matter up, but never did so. He renewed his notes, which were due on demand, April 1, 1928, but gave the bank no collateral. Things ran along and later he put a mortgage upon his last three unencumbered farms, aggregating in the neighborhood of $122,000. In order to procure excess loans, he used the name of his son and son-in-law and others, supplying collaterals as security therefor. After putting a mortgage upon his last three unencumbered farms he was still in straightened circumstances. In July, [fol. 19] 1928, the son's note became due, was renewed and fresh collaterals deposited with it, the collaterals being the bankrupt's.

In August the bank loaned Fitzgerald $5,000, which was to be replaced the next day, to take to Peoria to use in closing a transaction. No note was taken for it ostensibly for fear a Bank Examiner might come to Pekin and find the excess loan. Fitzgerald did not return the money the next day, nor for several days, notwithstanding the fact he had been requested to do so, but failed in this regard. There was also due $644, interest on the note of the bankrupt's son which had been paid by the bank and for which the bank had asked for a check. This matter hung fire from the 13th of August until September 1st, when Mr. Sipfle asserted the bank's common law lien upon the bankrupt's deposit and appropriated $5644 to the bank. At the close of business Mr. Sipfle poked a debit memorandum through the letter hole in the door of Mr. Fitzgerald's office.

The checks involved in the second cause of action had been issued by Fitzgerald and sent to the payees. He had undoubtedly expected the balance which he had in the bank to be sufficient to take care of those two checks when they arrived, and the appropriation of the $5644 interfered with his arrangement and created the situation involved in the second cause of action. This also showed that Fitzgerald had not intended to pay the money which he had borrowed from the bank and for which he had given no note. In the thirty-five years of Fitzgerald's relations with the bank his checking account had never been subjected to the common law lien of the bank. It is apparent in the light of the close relations which existed between Fitzgerald, Sipfle, Reiss and Mott, the cashier, that the procedure was very unusual and shocking and when Sipfle forced the transaction whereby Fitzgerald's son-in-law Barnes gave his note for $8,000 and collaterals therefor by the bankrupt, other officers of the bank remarked that the president was going to stand by his extraordinary procedure in appropriating the deposit of Fitzgerald. Mr. Sipfle probably knew more about the bankrupt's personal affairs and securities than any other one person.

All of these things were very minutely considered by the Master; he saw and heard the witnesses testify. Judge Black testified that in May, 1928, he had talked with the bankrupt's son-in-law, George Barnes, and told him there were several situations in which trouble had arisen in Fitzgerald's making payments; that he had asked Fitzgerald to [fol. 20] give him a complete statement of his financial affairs, but was unable to get one, Mr. Barnes told Judge Black he had heard a rumor that Fitzgerald's condition was a little shaky and asked him to get a financial statement. The same two gentlemen had another conversation in August, 1928. Mr. Barnes said: "I knew myself Mr. Fitzgerold was having some difficulties in regard to disposing of farms that he had taken over as trustee for bondholders. I also knew from conversations I had had with Judge Black and others that some of the transactions were somewhat irregular and that the situation had become quite serious. I went to Judge Black and almost demanded that he go to Mr. Fitzgerald and demand a complete financial statement to see if there was not something that could be done to relieve the pressure. I think I also said at that time that I

did not think Mr. Fitzgerald was insolvent, but that the matter needed immediate attention or he would be."

Here were two persons who would know only what Mr. Fitzgerald, the bankrupt, chose to tell them, particularly his attorney, when seeking advice or counsel upon some particular thing. The son-in-law Barnes, who would naturally be optimistic concerning his father-in-law's affairs, and yet, as early as May he heard a rumor that his father-in-law's condition was a little shaky and later appealed to the lawyer to do something to relieve the tension, which must have been great to cause him to say he had learned through Judge Black and others that his father-in-law's transactions were "somewhat irregular". In addition to this, some matters were getting into the hands of Lawyers and they were demanding settlements and threatening proceedings.

The president of the bank testified that beginning July 1st, the officers of the bank watched Fitzgerald's account very closely. The Master called attention to an aggregate of claims of $29,917.97 which, after that time, had gotten into the hands of the lawyers and were put through the bank. The bank also knew that he had been taking over farms on which he had mortgages; that when interest payments to many of his investors became due and borrowers were unable to pay their interest, that he paid it for them. It would be but natural that the rumors of irregularities described by his son-in-law would first reach the bank. Of course, Fitzgerald's lawyer, his bankers and his own son-in-law would be the last persons to believe Fitzgerald insolvent except upon a trial balance of Fitzgerald's busi-
[fol. 21] ness based upon an accurate appraisement.

But the law does not require that they should know absolutely he was insolvent. All that was necessary was the bank should know sufficient to put it upon inquiry, and knowing such facts, they were bound by all they would learn upon diligent inquiry. A diligent inquiry would have disclosed that Mr. Fitzgerald was hopelessly insolvent.

On the question as to whether or not the defendant bank had collateral security for the $26,000 straight promissory notes, Mr. Fitzgerald testified that the bank never had any collateral security of any kind for his straight promissory notes aggregating $26,000 until it was given to Mr. Spifle,

the president, on September 7th, or the 17th, whichever the correct date is. (Witnesses disagreed as to the date.)

Mr. Spifle testified that the bank had had collateral deposited with it to secure the payment of the Fitzgerald straight promissory notes, claiming to have gotten some $16,000 worth in June and some more in July. Upon his examination, Mr. Sipfle was asked this question:

"You said in your previous examination, as I recall it, you took all the collateral which John Fitzgerald had at that time, on the 7th of September, and he not having enough to take care of the $26,000 notes, he gave you the $3,000 of bank stock. Now I want you to enumerate, if you can, any collaterals which John Fitzgerald had left in his possession, there in his safe or in his possession otherwise, after you got your collateral securing the $26,000?

"Mr. Black: We object to that. How could he know?

"Witness: I can answer it partly and will be willing. I returned to him the discounts and the collaterals we had on the Edwin Fitzgerald note and other paper. In the exchange we made that day he offered me some of his own farm loans he had in his safe at that time and some other papers, some Jones and some Jenkins. I said we had sufficient Jenkins and we had one Jones, I think, being collateral outside our own county and we could not take his own farm loans. He had other papers in his hands but I couldn't tell exactly what they were. In his handling of those and shuffling over, it then looked to me like he had thirty or forty separate and distinct farm loan papers. I do know he had some of his own farm loans which I wanted and could not take, and did not."

[fol. 22] "Collateral security," given by a debtor is technically known in the law as the giving of a pledge. The necessary elements of a pledge are (1) a pledgor and a pledgee; (2) a debt or an obligation; and, (3) a contract of pledge. In re Evans, 238 Fed. 543; United Auto Co. v. Henderson, Auto Co., 207 S. W. 137 (Ark.).

There must be a contract whereby the property is to be held as security and this contract must clearly appear from the evidence. A contract of pledge is not constituted by a

mere loose understanding or statement or by statements by one party to which the other does not assent.

Mr. Sipfle also testified with reference to collaterals which he claims to have had for the bank:

"A. We had carried for him (the bankrupt), under discount, notes of Phil Imig, Thomas Murphy, Valentine Myers, Lizzie Zorel and Howard Graff.

"Q. You had those notes under discount. That had had nothing to do with the $26,000 loan?

"A. No, sir. That day he arranged to pay off those discounts. He had been selling some farm loans and with the proceeds, on the 15th and 16th he paid those off including the Murphy loan, and he left these discounts with us.

"Q. And according to your figures that aggregates $16,510.40?

"A. It should. Yes, sir. Those entries are shown here on the sheet of Mr. Fitzgerald's in the liability register, which is carried over by one of the clerks.

"Q. Go ahead with the July 24th item.

"A. The Phil Imig item, dated September 11th, 1926, due December 15th, 1927, amount $7500. On July 24th that was turned over to us. * * *

"A. Strother Wendroth, dated July 15th, 1927, due September 15th, 1927, amount $2550. That also came into our possession on July 24th.

"Q. Give the circumstances under which you obtained these notes on July 24th, 1928.

"A. *Those were collateral notes to his son, Edwin's note.* And in renewing that note and substituting other collateral he left this with us on July 24th.

"Q. Did you have any written agreement with John Fitzgerald either in June or July, say the 15th or 16th of June or 24th of July, with reference to your holding these [fol. 23] various notes as collateral security for this $26,000 debt.

"A. No, sir.

"Q. Well, did you have any verbal agreement?

"A. Yes, sir.

"Q. Well, tell us what the verbal agreement was—what the conversation was, who it was had with and where.

"A. Well, I don't know any particular date or any particular conversation, at first.

"Q. That would be in June, you mean?

"A. Yes, or anywhere along prior to June * * * and when he recorded the first trust deed he told the Committee, and others of the directors, that he would secure us. * * *

"Q. He would secure the $26,000?

"A. Yes, sir. * * *

"Q. Yes. That first trust deed was given, was it, May 22nd, 1928 and recorded June 13th, 1928, and is on Mackinaw Valley No. 1, Edward J. Cullihan to John Fitzgerald, Trustee?

"A. That is the first notice we had of it, yes. I don't know just the order, but that was one of them."

Mr. Sipfle said that he spoke to Mr. Fitzgerald about the exchange of collaterals; that the latter offered him again some of the loans that he had made on his own land and he told Mr. Fitzgerald he would rather have those than most anything. He then said if they had them as collateral to his own note they would be thrown out. "And we made an exchange. That is, I took all the collateral he had at the time and turned over what we had. He didn't have enough to give us sufficient collateral. He said: 'What I better do, I better resign.' I said: You better give me the ten shares of stock you have. I said: 'We can take that as collateral.' I said: 'You understand that ordinarily you are entitled to ten shares of stock, but if it is put up in any form as collateral security, you are out as a director, automatically.' "

Mr. Sipfle testified that at no time prior to September 7, 1928, did he ask John Fitzgerald for a statement of his liabilities and assets; that the notes in question were not secured at any time until the month of June, 1928. It was suggested to Mr. Sipfle that his claim was that on the 15th or 16th of June, 1928, John Fitzgerald left with the bank certain collateral to secure these three notes, aggregating [fol. 24] $26,000. That he was asked: "Why was it, if that is true, that you did not require John Fitzgerald to give a new note at that time using your regular collateral form note?" To which he answered: "John Fitzgerald was on the beginning of the sale of some of his farms. He told us he had made the sale to Ed Cullinan. He had other sales lined up and in view and it was his intention, and our thought, that he would be reducing the line and paying

off." He was then asked if that was the only explanation he had as to why he did not take a collateral note. He answered: "I have no other thought about it now."

He could give no conversation he had held with John Fitzgerald, or that he heard with other persons, representing the bank, and John Fitzgerald at any time with reference to his leaving the collaterals in question with the bank to secure the $26,000 loan. He replied: "I could not remember any specific conversation. The request would be made by me in the regular course of business." He was asked this question: "That request had been made a considerable length of time previous to the 24th of July, 1928, had it not?" and Mr. Sipfle answered: "It was made regularly and almost continually from the time he actually made his first sale or recorded a mortgage." When asked, what, if any, record of the bank he could produce showing that the bank held this collateral to John Fitzgerald's $26,000 indebtedness to the bank in either the month of June or July, 1928? he answered: "We have no record of that time." Then he was asked: "And no record of collaterals being held to secure this indebtedness was made by your bank until the month of September, 1928, isn't that true?", and the answer was: "That is the record that we have on our books; yes, sir."

The mere fact that a witness has been convicted of a felony does not disqualify him as a witness. The fact of conviction may always be shown to determine the degree of credibility to be accorded to him as a witness, and it doesn't appear that the Master gave any undue credence to the testimony of Mr. Fitzgerald, except to the extent that it was corroborated by other credible witnesses, such as Mr. Sipfle, the president of the bank, and Mr. Mott, the cashier, to say nothing of the records of the bank.

In one instance a number of collaterals which had been rediscounted were paid and the notes left in the bank. When Edwin Fitzgerald's note was due it was renewed and new collateral supplied and the old collateral left with [fol. 25] the bank. Mr. Sipfle said himself: "I returned to him the *discounts* and the *collateral we had on the Edwin Fitzgerald note and other paper.*" If that statement is true, it falls far short of showing that he returned the rediscounts and the collaterals which the bank held as secu-

rity for the John Fitzgerald $26,000 straight promissory notes.

The tone and attitude of the bank shown by the testimony of Mr. Sipfle himself, when asked why he did not require Mr. Fitzgerald to execute a regular collateral form note, which was: "John Fitzgerald was on the beginning of the sale of some farms of his. He told us he had made the sale to Ed Cullinan. He had other sales lined up and in view and *it was his intention, and our thought, that he would be reducing the line and paying off.*" In other words, until the climax came which resulted in the transactions involved in this case, on the 1st and 6th days of September, 1922, the belief was that he had made a sale, had other sales lined up and in view and it was his intention and the bank's thought that he would not execute any collateral contract but would "be reducing the line and paying off".

In other words, according to the testimony of the defendant's president, the records failed to show any entry in any of the bank's books that any contract of pledge had been made between John Fitzgerald and the bank until on or soon after September 7, 1928.

The transaction with reference to collaterals which took place, according to Mr. Sipfle, on September 7, 1928, was not a summary affair, because he said he "had volunteered to act, and had been in conference with him at least two or three days in the first week in September. He sat with us in Committee and Board meetings and we had him check up papers for us. He gave us information and told us he was telling us the truth and we were backing him up. I didn't take the bank stock then. I thought John Fitzgerald was a banker. I said: 'We have helped you out and we can help you out with this if you will freshen these up and we can help you get out!' " This was on the 7th of September, and then Mr. Sipfle testified: "and he said: 'I better give you the bank stock'. I said: 'All right'." So that after two or three days discussion of the matter and the checking up of the papers, Fitzgerald did not have enough collateral to secure the notes aggregating $26,000 by $3,000, and the bankrupt's ten shares of stock were taken as $3,000.

And, so, it is not material whether the witness Fitzgerald told the truth or not when he said he gave the last col- [fol. 26] laterals he had to the president of the bank and said: "I am done for; I have no money and no collaterals", for such was the fact, as established by the testimony of Mr. Sipfle.

If the officers of the bank knew no more that the current rumors as far back as in May that John Fitzgerald's condition was shaky when he mortgaged his last three unencumbered farms, his credit was not only slightly affected, but his ship was sinking, and then when the rumors of irregularities were afloat in the community, which finally found crystalization in a number of criminal indictments, the bank was chargeable with such knowledge as careful inquiry into Fitzgerald's solvency would produce.

Defendant's exception to the report of the Master as to the third cause of action must be denied, and the order will be: "Exceptions to Master's Report Overruled", and it is so Ordered.

[File endorsement omitted.]

IN UNITED STATES DISTRICT COURT

ORDER OVERRULING EXCEPTIONS TO MASTER'S REPORT, ETC.— Filed June 17, 1932

(Caption)

This cause coming on to be heard upon the exceptions of the plaintiff and the exceptions of the defendant to the first and second reports of the Special Master herein; and the Court having heard the arguments of counsel and being fully advised in the premises, finds: That the exceptions to the respective reports are without merit, and on consideration thereof, it is

Ordered, That all of the exceptions to the Special Master's reports be, and are hereby overruled, and a decree in harmony with the findings and holdings of the Special Master may be prepared and submitted.

Louis FitzHenry, Judge.

[File endorsement omitted.]

[fol. 27] IN UNITED STATES DISTRICT COURT

DECREE—Filed June 24, 1932

(Caption)

Suit to Recover Preference, etc.

At Peoria, in said District and Division, on the 24th day of June, A. D. 1932, before the Hon. Louis FitzHenry, Judge of said Court:

The Court having had this cause under advisement on Exceptions of the plaintiff and the defendant to the Reports of the Special Master in Chancery herein, and the Court having on 17th day of June, A. D. 1932, entered an Order herein overruling all Exceptions to the said Reports of the said Special Master in Chancery, and directed that a decree in harmony with the findings and holdings of said Special Master be prepared and submitted to the Court,

It Is, Therefore, Ordered, Adjudged and Decreed by the Court that the defendant, The Farmers National Bank of Pekin, Illinois, (A Corporation, organized under the National Banking Laws of the United States of America), be, and it is hereby, ordered and directed to forthwith turn over and deliver to the plaintiff herein the following notes or bonds received by the said defendant from John Fitzgerald, Bankrupt, on or about the 7th day of September, 1928, by way of unlawful or recoverable preference, to wit:

Phillip Imig Bond, numbered 7832, for $1,000.00, dated June 1, 1925, due Mar. 1, 1928, bearing 6% interest per annum, payable semi-annually, secured by Trust Deed of Phillip Imig, Widower, to John Fitzgerald, Trustee, encumbering the Southwest Quarter of Section Thirteen (13), Township Twenty-three (23) North, Range Two (2), West of the Third Principal Meridian, containing One Hundred and Sixty Acres (160), situated in Tazewell County, Illinois;

Phillip Imig Bond, numbered 7907, for $1,000.00, dated June 1, 1925, due Mar. 1, 1928, bearing 6% interest per annum, secured by Trust Deed of Phillip Imig to John Fitzgerald, Trustee, encumbering the East Half (E½) of [fol. 28] Section Fifteen (15), and the West Half (W½)

of the Southeast Quarter (SE¼) of Section Ten (10), Township Twenty-three (23) North, Range Two (2), West of the Third Principal Meridian, Tazewell County, Illinois;

Bond of Valentine Myers and Lena C. Myers, numbered 6696, for $1,000.00, dated Feb. 10, 1921, due March 1, 1926, bearing 6% interest per annum, secured by Trust Deed of Valentine Myers and wife, to John Fitzgerald, Trustee, encumbering the East Half (E½) of the West Half (W½) of Section Five (5), also Fifty-six (56) acres off the North Side of the Northwest Quarter (NW¼) of Section Nine (9), Township Twenty-three (23) North, Range Two (2), West of the Third Principal Meridian, containing Two Hundred and Sixteen (216) acres, situated in Tazewell County, Illinois;

First Mortgage Bond of Mary Graff, No. 7412, for $1,000.00, dated Mar. 1, 1924, due March 1, 1929, bearing 5½% interest per annum, secured by Trust Deed, to John Fitzgerald, Trustee, encumbering the Southeast Quarter (SE¼) of Section Thirty-One (31), Township Twenty-three (23), and the East Half (E½) of the Northwest Quarter (NW¼) of Section Six (6), Township Twenty-two (22) North, Range Two (2), West of the Third Principal Meridian, containing Two Hundred and Forty (240) Acres, situated in Tazewell County, Illinois; Bond signed by Mary Graff, Howard H. Graff, Mabel Cremeens, Harvey J. Graff and Elton C. Graff;

Mortgage Bond of George Z. Barnes and Mary F. Barnes, numbered 8215, for $500.00, dated Jan. 7, 1927, due Mar. 1, 1932, bearing 5½% interest per annum, payable annually, secured by Trust Deed to John Fitzgerald, encumbering the South Half (S½) of the Southeast Quarter (SE¼) of Section Twenty-Nine (29), also the Southeast Quarter (SE¼) of the Southwest Quarter (SW¼) of Section Twenty-Nine (29), all in Township Twenty-four (24) North, Range Three (3), West of the Third Principal Meridian, containing One Hundred and Twenty (120) Acres, situated in Tazewell County, Illinois;

Nine First Mortgage Bonds of Walter Jones, numbered 7540, 7541, 7572, 7573, 7574, 7575, 7576, 7578, and 7579, each for $1,000.00, each dated Sept. 1. 1924, each due Sept. 1, 1926, each bearing 6% interest per annum, payable annually, secured by Trust Deed on following described property: West Half (W½) and Part of the West Half (W½) of Southeast Quarter (SE¼) of Section Thirty-

[fol. 29] Two (32); South Half (S½) of Southwest Quarter (SW¼) of Section Thirty-three (33), Township Four (4), Range Seven (7); Northeast Quarter (NE¼) and North Half (N½) of Southeast Quarter (SE¼) of Section Five (5); Southwest Quarter (SW¼) and Part of Southeast Quarter (SE¼) of Section Four (4), Township Five (5), Range Seven (7), West of the Fourth Principal Meridian, containing Eight Hundred and Fifty (850) Acres, situated in Pike County, Illinois;

First Mortgage Bonds of Elmer V. Veesaert and Emma M. Veesaert, numbered 8452, 8456, 8457, 8458, and 8459, each for $1,000.00, each dated Mar. 1, 1928, each due Mar. 1, 1933, bearing 5½% interest, per annum, payable annually, and each secured by First Mortgage on an undivided one-half interest in 780 acres of land, situated in Madison County, Illinois, the other undivided one-half interest in 780 acre-tract being owned by the Estate of Henry Rose, Deceased, late of Tazewell County, Illinois;

Bond of Valentine Myers and Lena C. Myers, numbered 6668, for $500.00, dated Feb. 10, 1921, due Mar. 1, 1926, extended to Mar. 1, 1929, bearing 6% interest per annum, payable annually, secured by Trust Deed of Valentine Myers and Lena C. Myers, his wife, to John Fitzgerald, Trustee, encumbering the East Half (E½) of the West Half (W½) of Section Five (5), also Fifty-six (56) acres off the North Side of the Northwest Quarter (NW¼) of Section Nine (9), Township Twenty-three (23) North, Range Two (2), West of the Third Principal Meridian, containing Two Hundred and Sixteen (216) acres, situated in Tazewell County, Illinois.

It Is Further Ordered by the Court that the said defendant pay to the plaintiff the sum of Seven Thousand Two Hundred Seventy Two Dollars and Seventy Six Cents ($7,272.76), the value of other personal property received by the said defendant from the said John Fitzgerald on the said 7th day of September, 1928, by way of unlawful or recoverable preference, and which said personal property has since the said 7th day of September 1928 been collected or otherwise converted into cash, as follows:

Amount collected by defendant Bank on Charles Graff note, April 12, 1929, principal and interest $3183.78
Amount collected by defendant Bank April 16,

1929, from W. C. Sommer, note, principal and interest $1058.98

Amount received by defendant Bank from sale of 10 Shares of John Fitzgerald's Bank Stock in defendant Bank, February 9, 1929, together with 3% dividend thereon $3030.00

[fol. 30] It Is Further Ordered by the Court that the said defendant pay to the plaintiff the further sum of Ten Hundred Thirty Three Dollars and Four Cents ($1033.04), interest on the said sum of Seventy Two Hundred Two Dollars and Seventy Six Cents ($7272.76) at the rate of 5% per annum from July 20, 1929, to June 17, 1932.

It Is Further Ordered by the Court that the Clerk of this Court tax the costs of this suit, including the costs shown by the Reports of the Special Master in Chancery herein, and the sum of Twenty Dollars ($20.00) for the plaintiff's attorneys' docket fee herein, and that the defendant pay the amount of the taxed costs herein.

And it now appearing to the Court that since this cause was taken under advisement by the Court, and on the 26th day of January, A. D. 1932, the Comptroller of the Currency of the United States of America has appointed Ross C. Adams, Receiver for said defendant, The Farmers National Bank of Pekin, Illinois, and that said Receiver has qualified and is now acting as such,

It Is, Therefore, Ordered by the Court that a certified copy of this Decree be sent by Registered Mail by the plaintiff to the said Comptroller of the Currency of the United States of America, addressed to him at Washington, D. C., and that said Receiver of said defendant Bank and said Comptroller perform all of the foregoing decree to be performed by the said defendant Bank, The Farmers National Bank of Pekin, Illinois, and that they forthwith deliver to the plaintiff herein the said notes and bonds which the Court has ordered the said defendant to turn over and deliver to the plaintiff, and that the said Comptroller make the aforesaid payments to the plaintiff herein in the due course of administration of the affairs of the said defendant Bank.

It Is Further Ordered that this Court retain all jurisdiction for such further proceedings as may be necessary to be

taken, if any, in reference to the performance or execution of this Decree.

Louis FitzHenry, Judge.

[File endorsement omitted.]

[fol. 31] IN UNITED STATES DISTRICT COURT

PETITION FOR RULE ON RECEIVER TO TURN OVER FUNDS TO PLAINTIFF—Filed Aug. 30, 1932

(Caption)

To the Honorable Louis FitzHenry, Judge of said Court:

1. Now comes Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, bankrupt, plaintiff in the above entitled cause, and respectfully shows unto Your Honor that in pursuance of the provisions of the Decree entered in the above entitled cause on the 24th day of June, A. D. 1932, he did, on the 27th day of June, 1932, send, by registered mail, to the Comptroller of the Currency of the United States of America a duly certified copy of said Decree, which said certified copy was received by said Comptroller of the Currency at Washington, D. C., on the 29th day of June, 1932, as is more particularly shown by a return-receipt now in the possession of your petitioner, and ready to be offered in evidence upon the hearing of this petition; that, thereafter, in the months of July and August, 1932, your petitioner, acting by and thru his attorney, Ira J. Covey, had several conferences with the Receiver for said Farmers National Bank of Pekin, Illinois, Ross C. Adams, and with his duly authorized attorney, Franklin L. Velde, of Pekin, Illinois; that the said Receiver refused to comply fully with the terms of said Decree, as is more particularly shown by a Stipulation entered into between your petitioner and the said Ross C. Adams, Receiver, as aforesaid, on the 26th day of August, A. D. 1932, a copy of which is hereto attached, marked "Exhibit 1", and made a part of this petition.

2. Your petitioner further represents that as found by said Decree entered in this proceeding on the 24th day of June, 1932, the said defendant Farmers National Bank of

Pekin, Illinois, on the 7th day of September, 1928, received from the bankrupt, John Fitzgerald, by ways of unlawful or recoverable preference, certain Bonds and Stocks which are particularly described in said Decree; that the Special Master in Chancery of this Court found and reported to [fol. 32] this Court that the said transfer of said collateral securities to the said defendant Bank on the said 7th day of September, A. D. 1928, was null and void, and should be set aside, and that such Report of said Master in Chancery was afterward approved by the Orders and Decree of this Honorable Court.

3. Your petitioner further represents that the said defendant Bank never at any time obtained title to any of said Bonds or Stocks described in said Decree, aggregating the face value of $26,000.00, but that the title and ownership thereof at all times remained in your petitioner for the use and benefit of the creditors of said estate in bankruptcy.

4. Your petitioner further represents that as shown by the said Report of said Special Master in Chancery the said defendant Bank on April 12, 1929, without the knowledge or consent of your petitioner, collected from Charles Graff, the maker of one of said promissory notes, so received by the said defendant Bank by way of unlawful or recoverable preference, for principal and interest of said note, the sum of $3,183.78; that the said defendant Bank on the 16th day of April, 1929, without the knowledge or consent of your petitioner, collected from W. C. Sommer, the maker of another of said promissory notes, so received by the said defendant Bank by way of unlawful or recoverable preference, for principal and interest of said note, the sum of $1,058.98; that as shown by the Report of said Special Master in Chancery the said defendant Bank on the 9th day of February, 1929, without the knowledge or consent of your petitioner, sold and converted into cash the ten (10) Shares of Stock issued by the defendant Bank to John Fitzgerald, which was received by the defendant Bank by way of unlawful or recoverable preference, for the sum of $3,030.00.

5. Your petitioner further represents that after the original Bill was filed herein against the said defendant Bank, and on or about the 13th day of December, A. D. 1930, the said defendant Bank, without the knowledge or consent of

your petitioner, collected through legal proceedings, the sum of $1,597.31 from Bonds signed by Elmer E. Veesart and Emma A. Veesart, numbered 8452, 8456, 8457, 8458 and 8459, for $1,000.00 each, which were received by the said defendant Bank by way of unlawful or recoverable preference, making the total amount received by the said defendant Bank prior to the appointment of a Receiver for said Bank, out of the collaterals received by said Bank by way of [fol. 33] unlawful or recoverable preference, the sum of $8,870.07, as is more particularly shown by Paragraph 9, page 4, of said Stipulation, marked plaintiff's "Exhibit 1".

6. Your petitioner further represents that on and continuously after April 11th, 1929, down to and including the day of the closing of said defendant Bank by the Comptroller of the Currency, on the 8th day of January, A. D. 1932, the said defendant Bank had on hand in cash in its said Bank more than the sum of $50,000.00, and that the said Receiver upon taking possession of the assets of said Bank obtained therefrom more than the sum of $50,000.00 in cash; that said Receiver now has possession of the funds received by the said defendant Bank, as aforesaid, from the sale or collection of the said notes, bonds or stock, which was received by the said defendant Bank from the said John Fitzgerald on September 7th, 1928, by way of unlawful or recoverable preference, and that the said Receiver now unlawfully withholds such funds from your petitioner and has refused and still refuses to turn over and deliver such funds to your petitioner, and that the said Receiver, Ross C. Adams, now, in legal effect, holds the said funds for your petitioner as Trustee ex maleficio.

7. Your petitioner further represents that the said Receiver, Ross C. Adams, by refusing to comply with the order of this Court, and by contesting the right of your petitioner to receive from the said Ross C. Adams, Receiver as aforesaid, the said funds now in possession and custody of said Receiver, has made himself, as such Receiver of the said Bank, a joint tort feasor with the said defendant Bank, and is now liable as such Receiver to your petitioner for the said sums of money so received by the said defendant

Bank, and the said Receiver, which rightfully belong to your petitioner, and is also liable to your petitioner, as such joint tort feasor, for interest on said sums for wrongfully retaining said sums, together with the court costs which have heretofore accrued herein, and which the Court has ordered the said defendant Bank and the said Receiver to pay.

8. Wherefore, your petitioner prays that the said Ross C. Adams, Receiver as aforesaid, be ordered and directed by this Honorable Court to turn over and deliver to your petitioner the said sum of Eight Thousand Eight Hundred Seventy Dollars and Seven Cents ($8,870.07), property of your petitioner which the said defendant Bank and the said Receiver are now wrongfully detaining from your petitioner, together with legal interest thereon from the date [fol. 34] said sums were so wrongfully received and retained by the said Bank and the said Receiver, together with the costs heretofore taxed by the Clerk of this Court, and the further costs of these proceedings; and that an Order may be entered herein requiring the said Ross C. Adams, Receiver as aforesaid, to answer this petition, by a short day to be fixed by the Court, and to show cause, if any he has, why the prayer of this petition should not be granted; and that your petitioner may have such other and further relief as equity may require and to Your Honor shall seem meet.

Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt. Ira J. Covey, E. L. Covey, Attorneys for Petitioner.

Duly sworn to by Edwin V. Champion. Jurat omitted in printing.

EXHIBIT 1 TO PETITION

(Caption)

Whereas, under date of the 24th day of June, A. D. 1932, the Honorable Louis FitzHenry, Judge of said Court, signed and caused to be entered a Decree providing that Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, should deliver to the plaintiff certain bonds or mortgage notes, particularly described in said Decree

and should also pay to said plaintiff the sum of Seven [fol. 35] Thousand Two Hundred Seventy Two Dollars and Seventy-six Cents ($7,272.76), together with interest on said sum, amounting to Ten Hundred Thirty Three Dollars and Four Cents $(1033.04), being interest at the rate of five per cent per annum from July 20, 1929, to June 17, 1932, and should also pay the costs of said proceeding taxed by the Clerk of said Court; and, Whereas, said defendant Bank was closed by the Comptroller of the Currency on the 8th day of January, A. D. 1932, and has continuously since been and now is under the control of the Comptroller of the Currency of the United States of America.

Now it is hereby Stipulated and Agreed by and between plaintiff and said Ross C. Adams, as such Receiver, as follows, viz:

(1) That said Receiver has delivered to said plaintiff the following bonds or farm mortgage notes, itemized in said decree, viz:

(1) Philip Imig Bond #7832 for $1000.00; that said bond or mortgage note is involved in the foreclosure suit of Squire, et al. v. Imig, et al., General Number 8716, pending in the Circuit Court of Tazewell County, Illinois, and that said plaintiff is hereby subrogated to all rights of said defendant Bank and of said Receiver in said cause No. 8716; and the receipt of said bond is hereby acknowledged by said plaintiff.

(2) Philip Imig Bond #7909 for $1000.00; that said bond or mortgage note is involved in the foreclosure suit of Gillan, et al. v. Imig, et al., General Number 8477, pending in the Circuit Court of Tazewell County, Illinois, and that said plaintiff is hereby subrogated to all rights of said defendant Bank and of said Receiver in said cause No. 8477; and the receipt of said bond is hereby acknowledged by said plaintiff.

(3) Valentine Myers and Lena C. Myers, Bond #6696 for $1000.00; said plaintiff is hereby subrogated to any and all rights of said Bank and of said Receiver in any litigation which may be pending or hereafter commenced relative to said bond; and receipt of said bond is hereby acknowledged by said plaintiff.

(4) Mary Graff Bond #7412 for $1,000.00; that said bond or mortgage note is involved in the foreclosure suit of

Birkey, et al. v. Graff, et al., General Number 8809, pending in the Circuit Court of Tazewell County, Illinois, and that said plaintiff is hereby subrogated to all rights of said defendant Bank and of said Receiver in said cause No. 8809. Said bond is in the possession of the Master in Chancery [fol. 36] of Tazewell County, Illinois, as an exhibit in said cause and is not now received by the plaintiff.

(5) Participation Certificate based upon and aeccpted in lieu of bond of George Z. Barnes and Mary F. Barnes, No. 8215 for $500.00. Said Participation Certificate is dated the 14th day of May, A. D. 1932; is signed by Charles M. Edwards, Carson Voigt and Frank E. Nafziger, and its acceptance in full satisfaction of said Bond No. 8215 has heretofore been approved in writing by said plaintiff and by the Comptroller of the Currency. Receipt of said Participation Certificate is hereby acknowledged by the plaintiff.

(6) Walter Jones Bonds #7540, #7541, #7572, #7573, #7574, #7575, #7576, #7578 and #7579, for $1000.00 each; that said bonds or mortgage notes are involved in the foreclosure suit of Arnold, et al., v. Jones, et al., pending in the Circuit Court of Pike County, Illinois, and said plaintiff is hereby subrogated to all rights of said defendant Bank and of said Receiver in said suit. Receipt of said nine bonds is hereby acknowledged by the plaintiff.

(7) Elmer V. Veesaert and Emma M. Veesaert Bonds No. 8452, 8456, 8457, 8458 and 8459, for $1000.00 each; these Bonds were involved in the foreclosure suit of Kirchert, et al. v. Veesaert, et al., recently pending in the Circuit Court of Madison County, Illinois.

Said defendant Bank on or about the 13th day of December, 1930, received the sum of Fifteen Hundred Ninety Seven Dollars and Thirty One Cents ($1597.31) in full of a pro-rata share of the proceeds of said foreclosure suit, based on said bonds, and issued its own certificate dated Dec. 13, 1930, payable to itself for said sum of Fifteen Hundred Ninety Seven Dollars and Thirty One Cents ($1597.31), which Certificate is now in the possession of said Receiver and is hereinafter referred to and accounted for. Receipt of the five Veesaert bonds is hereby acknowledged by the plaintiff and he is hereby subrogated to any

and all rights of said defendant Bank and of said Receiver in said litigation.

(8) Valentine Myers and Lena C. Myers, Bond #6668 for $500.00. Said plaintiff is hereby subrogated to all rights of said defendant Bank and of said Receiver in any litigation which may be pending or hereafter commenced relative to said bond; and receipt of said bond is hereby acknowledged by said plaintiff.

(9) Said defendant Bank, in addition to the proceeds of said Vessaert notes as hereinbefore set forth, collected dur-
[fol. 37] ing the pendency of this litigation, the following amounts as set forth in said Decree, dated the 24th day of June, A. D. 1932, viz:

Charles Graff note, principal and interest	$3183.78
W. C. Sommer note, principal and interest	$1058.98
Proceeds of sale of ten shares of John Fitzgerald Bank Stock in defendant Bank, including dividend thereon	$3030.00
Total	$7272.76
to which should be added the proceeds of said Veesaert notes	$1597.31
Grand Total	$8870.07

It Is Further Stipulated and Agreed that the delivery by said Receiver and the receipt by said plaintiff of said bonds and said Participation Certificate and the subrogation of the plaintiff to the rights of said defendant Bank and of said Receiver in and to all litigation now pending or which may hereafter be begun in reference to said bonds or any or either of them, or in reference to said Participation Certificate, is accepted by said plaintiff as a full compliance on the part of said defendant Bank and of said Receiver with the terms and provisions of said decree, dated the 24th day of June, A. D. 1932, with the exception of the payment of said sum of Eight Hundred Seventy Dollars and Seven Cents ($8870.07); with the further exception of interest on said item and with the still further exception of the costs of this litigation.

It is contended on behalf of the plaintiff that said sum of Seven Thousand Two Hundred S-venty Two Dollars and Seventy Six Cents ($7,272.76), together with interest thereon from the 20th day of July, 1929, to June 24, 1932, should be allowed as a preferred claim and be paid at once in full, out of the assets in the hands of said Receiver and that said sum of Fifteen Hundred Ninety Seven Dollars and Thirty One Cents ($1597.31), being the proceeds of said Veesaert notes as hereinbefore set forth), together with interest thereon at the rate of 5% per annum from the 13th day of December 1930, being the date of the receipt thereof by said defendant Bank), to the 24th day of June, 1932, should also be allowed as a preferred claim and be paid at once in full out of the assets in the hands of said Receiver.

[fol. 38] It is the contention of said Receiver that any claims allowed against him herein and any payments ordered herein to be made by him should be ordinary and unpreferred claims and that no interest on said amounts should be allowed after the 6th day of January, A. D. 1932, being the date on which the Comptroller of the Currency took possession of said defendant Bank.

It is the contention of plaintiff that said Receiver is liable for the costs of this litigation, which have been taxed by the clerk of this court in pursuance to said Decree.

It is the contention of the Receiver that as he was not made a party to this cause, that no costs should be awarded or allowed against him, and that if the Court holds that the costs of this litigation as taxed by the Clerk should be assessed against the Receiver, that they should be allowed as an ordinary and unsecured claim against the assets in his hands on which said claimants should receive dividends only, and not payment in full.

It is further agreed that either said plaintiff or said Receiver may apply to said Court for a decision and decree as to any matter in dispute herein, as hereinbefore set forth and that reasonable notice be given the adverse party of any such litigation.

Executed this 26th day of August, A. D. 1932.

(Signed) Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt, Plaintiff.

Approved:

Ira J. Covey, Attorney for said Plaintiff. (Signed) Ross C. Adams, Receiver of Farmers National Bank of Pekin, Illinois.

Approved:

Velde & Prettyman, Attorneys for said Receiver, by Franklin L. Velde.

[File endorsement omitted.]

[fol. 39] IN UNITED STATES DISTRICT COURT

ORDER REQUIRING RECEIVER TO ANSWER PETITION, ETC.—
Filed Aug. 30, 1932

(Caption)

Before the Honorable Louis FitzHenry, Judge of Said Court

This cause coming on now to be heard upon the Petition of Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, bankrupt, plaintiff in the above entitled cause, asking for an order on Ross C. Adams, Receiver of Farmers National Bank of Pekin, Illinois, the above named defendant, to turn over and deliver to the plaintiff Eight Thousand Eight Hundred Seventy Dollars and Seven Cents ($8,870.07), alleged to be the property of the plaintiff, together with legal interest thereon from the date said sums are alleged to have been wrongfully received and retained by said Bank and its Receiver, together with the costs heretofore taxed by the Clerk of this Court, and the further costs of these proceedings, and it appearing to the Court from a Stipulation entered into in the above entitled cause between said plaintiff and the said Ross C. Adams, Receiver of said Bank, dated the 26th day of August, A. D. 1932, copy of which said Stipulation is attached to said plaintiff's Petition, and made a part thereof, that it was agreed between the said plaintiff and said Receiver as follows:

"It Is Further Agreed that either said plaintiff or said Receiver may apply to said Court for a decision and decree

as to any matter in dispute herein, as hereinbefore set forth, and that reasonable notice be given the adverse party of any such litigation."

It Is Therefore, Ordered by the Court that the said Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, be, and he is hereby, ordered to answer said plaintiff's Petition within thirty (30) days from the date [fol. 40] of the entry of this Order, and show cause, if any he has, why the prayers of said Petition should not be granted.

Entered this 30th day of August, A. D. 1932.

Louis FitzHenry, Judge.

[File endorsement omitted.]

In United States District Court

(Caption)

Answer of the Respondent, Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, to the Petition of Plaintiff—Filed Oct. 4, 1932

This respondent answering says:

(1) That the Farmers National Bank of Pekin, Illinois, as an insolvent bank, went into possession and control of the Comptroller of the Currency of the United States of America at the close of business on the 7th day of January, A. D. 1932; that this respondent was appointed as receiver of said bank by the Comptroller of the Currency of the United States of America on the 26th day of January, A. D. 1932; that prior to the 26th day of January, A. D. 1932, this respondent had no knowledge whatever as to this litigation or any of the facts relating thereto; and that such information as he now has has been acquired since the 26th day of January, A. D. 1932 and that this answer is therefore, largely based upon information and belief.

(2) That so far as this respondent is advised, he was never formally made a party to this suit and is not now a party thereto; that this respondent had no official knowledge relating to this suit until—soon after the 24th day of

[fol. 41] June, A. D., 1932—he was served with a copy of the decree entered herein on the 24th day of June, A. D., 1932 and referred to in the petition to which this is an answer.

(3) That as will appear from the stipulation, marked Exhibit 1, attached to the pending petition and made a part thereof, this respondent has fully complied with said decree entered on the 24th day of June, A. D., 1932, with the exception of the payment of the sum of eight thousand, eight hundred seventy dollars and seven (-8,870.07) cents referred to in said petition and with the exception of the payment of the interest on said sum and with the further exception of the payment of any of the costs of this suit.

(4) This respondent shows to the court that said entire sum of eight thousand, eight hundred seventy dollars and seven ($8,870.07) cents was collected by said bank long prior to the entry of said decree so entered on the 24th day of June, A. D., 1932 and long prior to the commencement of the April term A. D., 1932 of this court; that fifteen hundred ninety-seven dollars and thirty-one ($1597.31) cents of said sum was collected by said bank after the filing of the bill of complaint herein; and that the remainder of seven thousand, two hundred seventy-two dollars and seventy-six ($7,272.76) cents was collected by said bank prior to the filing of the bill of complaint herein; and that as this respondent is informed and charges the fact to be, said bank and its officials claimed that at the time said seven thousand, two hundred seventy-two dollars and seventy-six ($7,272.76) cents was collected, said bank and its officials believed that said sum of seven thousand, two hundred seventy-two dollars and seventy-six ($7,272.76) cents belonged to said bank and not to the plaintiff herein.

(5) That the bill of complaint herein was not filed until the 20th day of July, 1929 and that all of said sum of seven thousand, two hundred seventy-two dollars and seventy-six ($7,272.76) cents was collected by said bank prior to the 17th day of April, 1929.

(6) That this respondent admits that the plaintiff is entitled to have said sum of eight thousand, eight hundred seventy dollars and seven ($8,870.07) cents allowed as an ordinary or unpreferred claim against said bank, together with interest on the respective amounts from the time of

their respective collection, at the rate of 5% per annum, up to the 8th day of January, A. D., 1932, being the day upon [fol. 42] which said bank passed into the possession and control of the Comptroller of the Currency of the United States of America.

(7) That this respondent specifically denies that the plaintiff is entitled to have said sum of eight thousand, eight hundred seventy dollars and seven ($8,870.07) cents or any part thereof allowed, as a preferred claim against said bank and the assets thereof.

(8) That this respondent denies that said bank on said 8th day of January, A. D., 1932 had in cash more than the sum of fifty thousand ($50,000,00) dollars, but avers that the cash on hand was less than twenty-seven thousand ($27,-000.00) dollars; and admits that the cash on hand in said bank on said 8th day of January, A. D., 1932, exceeded said sum of eight thousand, eight hundred seventy dollars and seven ($8,870.07) cents and the interest thereon, as claimed by the plaintiff.

(9) This respondent further answering admits that he withholds and refuses to turn over said sum of eight thousand, eight hundred seventy dollars and seven ($8,870.07) cents, but avers that he does not do so willfully; but that he does not feel justified or authorized to make payment of said sum or any part thereof, until it is determined by this court whether said claim of the plaintiff is a preferred claim or whether it is an unpreferred claim and must share pro rata with the claims of the other unpref*f*ered creditors of said bank.

(10) This respondent specifically denies that he holds said funds or any portion thereof as a trustee ex maleficio and denies, on information and belief that said bank held said funds or any portion thereof as a trustee ex maleficio.

(11) This respondent further answering, denies that the plaintiff is entitled to any interest on said funds or any of them up to any later date than said 8th day of January, A. D., 1932.

(12) This respondent further answering says that so far as he is advised, none of the costs of this proceeding have been incurred by this respondent, but that all of said costs—

or substantially all of them—accrued during the defense by said bank of the claim of the plaintiff herein; and this respondent contends that any costs taxed against said bank herein should be allowed as an ordinary and not a preferred claim against said bank and the assets thereof.

(13) And now having fully answered said petition, this respondent prays that he may be hence dismissed with his [fol. 43] reasonable costs and charges in this behalf most unjustly sustained.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois. Velde & Prettyman, Attorneys for Said Receiver, by Franklin L. Velde.

Duly sworn to by Ross C. Adams. Jurat omitted in printing.

[File endorsement omitted.]

In United States District Court

Order Granting Leave to File Amended Answer—Entered Oct. 26, 1932

Comes now the Receiver of the Farmers National Bank of Pekin, Illinois, Ross C. Adams Esq., and on his motion leave is hereby granted to the said Receiver to file an amended answer herein by October 31, A. D. 1932.

[fol. 44] In United States District Court

Order Granting Leave to File Amended Answer—Entered Oct. 31, 1932

Come now Messrs. Velde & Prettyman, attorneys for Ross C. Adams, Receiver for the Farmers National Bank of Pekin, Illinois and on their motion, leave is hereby granted to the said Receiver to file an amended answer by November 7th, A. D. 1932.

IN UNITED STATES DISTRICT COURT

(Caption)

AMENDMENT OF ANSWER OF RESPONDENT, ROSS C. ADAMS, RECEIVER OF THE FARMERS NATIONAL BANK OF PEKIN, ILLINOIS, TO THE PETITION OF THE PLAINTIFF—Filed Nov. 11, 1932

By leave of Court first had and obtained, this respondent amends his answer filed herein on the 4th day of October, A. D. 1932 by adding thereto a paragraph to be numbered 7-a and to be inserted immediately after paragraph No. 7 of his said answer, viz:

(a) The payment of ten hundred fifty-eight dollars and ninety-eight ($1058.98) cents on April 16, 1929 (being $1,000.00 principal and $58.98 interest for the W. C. Som- [fol. 45] mer collateral) did not result in any augmentation of the funds or assets of said bank, so far as this respondent has been able to ascertain up to this time from an examination of the books, records and files of said bank; that this respondent has been unable to definitely determine whether said sum of ten hundred fifty-eight dollars and ninety-eight ($1058.98) cents was paid by said Sommer from money on deposit in said Farmers National Bank or from money borrowed for the purpose by said Sommer from said Farmers National Bank; or whether said payment was made by checks of others drawn on other banks and ultimately deposited with the first National Bank of Peoria or with the Merchants and Illinois National Bank of Peoria. The facts relative to the lowest amount of deposit thereafter of said Farmers National Bank with said First National Bank of Peoria and with said Merchants and Illinois National Bank of Peoria are set forth in subdivision "C" of this amended answer; and that the burden of tracing said Sommer payment is on the plaintiff and not on this respondent.

(b) The payment of fifteen hundred ninety-seven dollars and thirty-one ($1597.31) cents in full of said Veeseart collateral was made by a draft remitted by said Farmers National Bank on December 13, 1930 to the First National Bank of Chicago and was credited by said First National

Bank of Chicago to said Farmers National Bank. Thereafter, on October 27, 1931, the total deposit of said Farmers National Bank with said First National Bank of Chicago was reduced to the sum of six hundred forty-three dollars and twenty-four ($643.24) cents; and therefore, the funds or assets of said Farmers' National Bank, which came into the possession and control of this respondent as such receiver would have been augmented in any event, only by said sum of six hundred forty-three dollars and twenty-four ($643.24) cents; but this respondent further avers that the entire credit balance of said Farmers National Bank with said First National Bank of Chicago was appropriated by said First National Bank of Chicago, when said Farmers National Bank was Closed by the Comptroller of the Currency and that no part of he credit of said Farmers National Bank with said First National Bank of Chicago ever came into the possession or control of this respondent; but that said First National Bank of Chicago appropriated the entire credit balance of said Farmers National Bank and applied it in part payment of [fol. 46] the indebtedness then owing from said Farmers National Bank to said First National Bank of Chicago.

(c) The payment of thirty-one hundred eighty-three dollars and seventy-eight ($3183.78) cents on April 12, 1929 (being three thousand ($3,000.00) dollars principal and one hundred eighty-three dollars and seventy-eight ($183.78) cents interest for the Charles Graff collateral), was part of a payment aggregating fourteen thousand, thirteen dollars and sixty-four ($14,013.64) cents deposited by said Graff or someone on his behalf in said Farmers National Bank in the form of drafts or checks, all of which were drawn on banks other than said Farmers National Bank; that some of said drafts or checks were deposited by said Farmers National Bank with the First National Bank of Peoria; some with the First National Bank of Chicago and the balance with the Merchants and Illinois National Bank of Peoria, which last mentioned bank was thereafter merged with the Commercial Merchants National Bank of Peoria.

That thereafter on November 28, 1930, the deposit of said Farmers National Bank in said First National Bank of Peoria was reduced to the sum of fifty-one dollars and forty ($51.40) cents; that on the 11th day of October, 1929,

the deposit of said Farmers National Bank with the First National Bank of Chicago was reduced to the sum of seventy dollars and fifty-four ($70.54) cents and (as hereinbefore averred) the entire credit balance of said Farmers National Bank with the First National Bank of Chicago was appropriated by said First National Bank of Chicago, when said Farmers National Bank was closed by the Comptroller of the Currency; this respondent further avers that the deposit of said Farmers National Bank with said Commercial Merchants National Bank was on the 29th day of December, 1931, reduced to the sum of three hundred fifty-one dollars and ninety-four ($351.94) cents; and that the payment of said Charles Graff collateral did not result in any augmentation of the funds and assets of the Farmers National Bank, coming into the possession and control of this respondent in excess of said fifty-one dollars and forty ($51.40) cents (being the minimum credit balance in said First National Bank of Peoria), plus said sum of three hundred fifty-one dollars and ninety-four ($351.94) cents (being the minimum credit balance in said Commercial Merchants National Bank), or the minimum credit balance in one of said banks, if the credit from said Graff payment is traced to one of said banks.

[fol. 47] This respondent further avers that although he has made diligent search and examination of the records and files of said Farmers National Bank, he has been unable thus far to ascertain whether said sum of thirty-one hundred eighty-three dollars and seventy-eight ($3183.78) cents (being payment of said Graff collateral and being part of a total payment of fourteen thousand, thirteen dollars and sixty-four ($14,013.64) cents, as hereinbefore set forth) was deposited in the First National Bank of Peoria or in the First National Bank of Chicago or in the Merchants Illinois National Bank, afterwards merged with the Commercial Merchants National Bank of Peoria; and that the burden of tracing said Graff payment is on the plaintiff and not on this respondent.

(d) That the sale of ten shares of bank stock of said Farmers National Bank referred to in said petition, for the sum of three thousand ($3,000.00) dollars, plus thirty ($30.00) dollars dividend thereon, did not result in any augmentation of the funds or assets of said bank, nor in

any augmentation of the funds or assets of said bank, which came into the possession or control of this respondent, as such receiver; but that said bank stock was sold to one R. A. Cullinan for the sum of three thousand ($3,000.00) dollars, who obtained the funds for the purchase of said bank stock by borrowing the full amount for said purchase from said Farmers National Bank.

This respondent further avers that he has been unable to find any entry in the books or files of said bank relating to said thirty dollar dividend, but that if said dividend was paid to said bank, it must have been paid out of funds of said bank and therefore did not result in any augmentation of the funds or assets of the bank, nor in any augmentation of the funds or assets of said bank, nor came into the possession or control of this respondent, as such receiver.

(e) This respondent therefore, claims and avers that the plaintiff herein is not entitled to the allowance of his claim or any part thereof, as a preferred claim against the assets or funds of said Farmers National Bank, which came into the possession or control of this respondent as such receiver.

(f) That the statements and averments contained in this amendment are based upon information gained by this respondent from the books, files and records of said Farmers National Bank and that this respondent has no other or different information or knowledge upon the subject; and that said books, files and records are hereby tendered to [fol. 48] the plaintiff and his attorney for examination at such reasonable times and places as may be agreed upon between them and this respondent or as may be directed by the court.

Respectfully submitted, Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois. Velde & Prettyman, Attorneys for Said Receiver, by Franklin L. Velde.

Duly sworn to by Ross C. Adams. Jurat omitted in printing.

[File endorsement omitted.]

[fol. 49] IN UNITED STATES DISTRICT COURT

(Caption)

Ira J. Covey, Esq., Peoria, Illinois, Appearing for the Plaintiff.

Franklin L. Velde, Esq., Pekin, Illinois, Appearing for Ross C. Adams, Receiver for the Farmers National Bank.

STIPULATION OF FACTS—Filed Dec. 28, 1932

Be It Remembered that heretofore on to-wit, the First Day of December, A. D. 1932, the same being one of days of the October A. D. 1932 Term of said Court, the above entitled cause came on for hearing before Honorable Louis FitzHenry, one of the Judges of said Court, whereupon the following proceedings were had, to-wit:

It Is Hereby Stipulated and Agreed by and between the plaintiff Edwin V. Champion, Trustee of the Estate of John FitzGerald, Bankrupt, and the respondent Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, defendant herein, as follows, to-wit:

That the Court may take judicial notice of all of the records and proceedings, orders, decrees, etc., in this case;

That a true and correct copy of the stipulation which was entered into between Edwin F. Champion, Trustee in Bankruptcy of John FitzGerald, plaintiff, and Ross C. Adams, Receiver as aforesaid, dated August 26, 1932, is attached to plaintiff's petition which was filed in this proceeding on August 30, 1932; that it was reported by the attorney for the plaintiff to the attorney for the defendant that said petition was filed on August 29, 1932, and that the date August 29, 1932, is used in the answer and amended answer of the defendant;

That on June 27, 1932, the plaintiff's attorney mailed to the Comptroller of the Currency of the United States at Washington, D. C. a certified copy of the decree entered by the Court in this cause on June 24, 1932, sending same by registered mail, and that the same was received by the said Comptroller of the Currency in due course of United States Mail;

That Plaintiff's Exhibit Number One is a true and correct statement of court costs in said Equity Cause Number 779, issued by the Clerk of this court; that the Court costs

[fol. 50] aggregating $1,629.80 shown by Plaintiff's Exhibit Number One were all incurred previous to the entry of the decree herein on June 24, 1932, and that the respondent Ross C. Adams, Receiver, did not in any way participate in this proceeding nor have any official notice thereof until after the entry of said decree on the 24th day of June, 1932; that said sum of $1,629.80 is allowable against the said receiver only as an ordinary and not as a priority claim; that interest at the rate of five per cent per annum shall be allowed on the various items in cash collected by said bank, aggregating the principal sum of $8,870.07 from the dates of the respective collections up to the 7th day of January 1932, and that the same is an unpreferred and not a preferred claim; unless there shall be sufficient funds in the hands of the receiver, after paying all claims against the bank in full, in which case the plaintiff is entitled to interest, pro rata with other creditors of the bank, from the date of January 7, 1932 down to the time of the payment thereof;

That the ten (10) shares of the capital stock of the Farmers National Bank of Pekin, Illinois, which is referred to on page five of said decree, were sold by said defendant bank on February 9, 1929, to R. A. Cullinan for the sum of Three Thousand Dollars, and that by said decree which is not appealed from, said bank obtained the further sum of Thirty Dollars in the nature of a dividend on said bank stock: that on February 9, 1929 said R. A. Cullinan borrowed from the defendant Farmers National Bank of Pekin, Illinois, Four Thousand Dollars ($4,000.00) for which said Cullinan gave his personal promissory note to said bank payable on demand in the sum of Four Thousand Dollars; that said promissory note was paid by said Cullinan to said bank as follows: $2,500.00 on June 28, 1929, and $1,500.00 on March 1, 1930: that on February 9, 1929 said Cullinan had been given credit on the books of the bank for the sum of Four Thousand Dollars which he had borrowed on that date; that the Three thousand dollars ($3,000.00) which said Cullinan paid for said ten shares of stock of the Farmers National Bank of Pekin, Illinois, was taken out of the Four Thousand Dollars credited to the said Cullinan by said bank on February 9, 1929 as the proceeds of his Four Thousand Dollar note; that the three thousand dollars paid by said

Cullinan for said ten shares of bank stock was taken from his account and was converted into and is represented by a certificate of deposit, No. 115504, of the Farmers National [fol. 51] Bank, of Pekin, Illinois, for the sum of Three Thousand Dollars, a true copy of which is marked Plaintiff's Exhibit Number Two, attached to and made a part of this stipulation;

That during the period of time from February 5, 1929 up to and including January 7, 1932, the lowest amount of cash and cash items in the tills of the Farmers National Bank, Pekin, Illinois, was the sum of $30,548.61, which amount said bank had on hand on September 3, 1931; that the amount of cash and cash items in said bank at the time of its closing on January 7, 1932 was the sum of $36,054.76; that said bank suspended at the close of business on January 7, 1932, and did not thereafter reopen;

That the Charles Graff note for Three Thousand Dollars principal and $183.78 interest, which is referred to on page 5 of said decree of the Court, was paid by said Charles Graff to said defendant bank on April 12, 1929, the total amount paid being $3,183.78;

That on April 12, 1929, said Charles Graff deposited with the Farmers National Bank, of Pekin, Illinois, the sum of $14,013.64 made up of five items as follows:

Item No. 1: A draft in the sum of $3,000.00 drawn on Central National Bank of Peoria, payable to W. Ernst, No. 52,400; the Farmers National Bank sent said draft to the First National Bank of Peoria for credit, the First National Bank of Peoria being one of the defendant bank's Peoria Correspondents; that said defendant bank was given credit by the said First National Bank of Peoria for said sum of $3,000.00; that on November 28, 1930, the low balance of the defendant bank in the said First National Bank of Peoria was $51.41; that on April 12, 1929, the credit balance of the defendant bank with said First National Bank of Peoria was $43,760.78; that said credit balance on each of the following dates was as follows:

1929	
April 13	$27,900.39
15	34,118.13
16	36,198.30
17	28,484.14
18	29,706.30

19	33,504.78
20	32,545.69
22	29,452.36
23	30,036.66

[fol. 52] Item No. 2: (In said Charles Graff transaction): Two drafts, one for $2,900.00, and one for $1,660.00, total $4,560.00, which said drafts were drawn by the American State Bank on the Illinois Merchants Trust Company and were sent by said defendant bank to the First National Bank of Chicago, for credit, said drafts being payable to the order of William Ernst; that the account of the said defendant bank with said First National Bank of Chicago on April 12, 1929 was given credit for the said sum of $4,560.00; that on October 11, 1929, the low balance of the said defendant bank in the First National Bank of Chicago was $70.54; that on the 12th day of April, 1929, the credit balance of the defendant $36,553.50; that said credit balance on each of the following dates was as follows:

1929	
April 13	$36,388.60
15	33,839.41
16	35,195.94
17	32,958.23
18	37,726.34
19	38,690.96
20	32,182.42
22	48,382.95
23	37,322.68

Item No. 3: (In said Charles Graff transaction): Said defendant bank received from said Charles Graff a check for $1,240.00 drawn by W. Ernst on the Liberty State Bank of Bloomington, Illinois; that this check was collected by the Bloomington Bank and that it set its draft No. 21,782 to the defendant bank, drawn on the Chicago Trust Company, for the sum of $1,239.50, having deducted fifty cents (50c) for exchange; that said defendant bank set this draft for $1,239.50 to the First National Bank of Chicago for credit on April 16, 1929, and on that day said defendant bank received a credit on the books of said National Bank of Chicago, in the sum of $1,239.50;

Item No. 4: (In said Charles Graff transaction): This was a check delivered to said defendant bank by said Charles Graff for the sum of $4,920.56, drawn by William Ernst on the Farmers State Bank of Carlock, Illinois; that this check was sent by the defendant bank to the Farmers State Bank of Carlock and said Carlock remitted to the defendant bank by draft No. 5,738 for $4,920.56, which draft [fol. 53] was drawn on the First National Bank of Joliet, Illinois; that this draft was sent by the defendant bank on April 13, 1929 to the First National Bank of Peoria for credit and said defendant bank on the 13th day of April 1929 received a credit on the books of said First National Bank of Peoria for the sum of $4,920.56;

Item No. 5: (In said Charles Graff transaction): The defendant bank on April 12, 1929, received a check from Charles Graff drawn by Harry Graff in the sum of $293.08, dated April 12, 1929, on the Hopedale National Bank, Hopedale, Illinois; that said check was forwarded by the defendant bank to the Hopedale National Bank for collection and that said Hopedale Bank sent its draft to the defendant bank, drawn on the Merchants & Illinois National Bank of Peoria; that this draft in the sum of $293.08 was sent by the defendant bank on April 13, 1929 to the Merchants & Illinois National Bank of Peoria for credit, and that said defendant bank on April 13, 1929, received a credit from said Merchants and Illinois National Bank for the sum of $293.08; that thereafter the Merchants & Illinois National Bank of Peoria merged with the Commercial National Bank of Peoria, and that the name of the merged or consolidated bank is Commercial Merchants National Bank and Trust Company of Peoria; that upon the merger of said Merchants & Illinois National Bank of Peoria with the Commercial National Bank of Peoria, the account of the Farmers National Bank of Pekin with the Merchants & Illinois National Bank of Peoria was transferred to and thereafter carried in the Commercial Merchants National Bank and Trust Company of Peoria; that the low balance of the defendant bank in said merged bank, on December 29, 1931, was $351.94; that the balance of the defendant bank in the Merchants & Illinois National Bank of Peoria on April 12, 1929, was $12,925.04; that said credit balance on each of the following dates was as follows:

1929	
April 13	$17,047.66
15	13,627.41
16	16,440.65
17	15,792.13
18	13,878.34
19	12,843.88
20	8,816.70
22	15,665.84
23	12,025.26

[fol. 54] That on April 12, 1929, the said defendant bank acting by and through T. W. Scott, its cashier, issued to Frank F. Reise, who was then vice president of said defendant bank, two certificates of deposit, one, No. 116,062, in the principal sum of $3,000.00, and the other, No. 116,063, in the sum of $183.78; that written on the lower left-hand corner of each of said certificates of deposit in the handwriting of said T. W. Mott appear the words "Chas. Graff"; that the said Frank F. Riese departed this life in the year 1931, and that thereafter his executors, by order of the County Court of Tazewell County, Illinois, on July 5, 1932, endorsed said certificates of deposit to the respondent Ross C. Adams, Receiver of said Defendant bank, a true copy of which said certificates of deposit and the endorsements thereon are attached to this stipulation and marked Plaintiff's Exhibits Three and Four, respectively, and made a part of this stipulation;

That the note of W. C. Sommer in the principal sum of One Thousand Dollars ($1,000.00) and interest of $59.98 which is referred to by the Court in its decree on page 5 thereof, was paid by the said W. C. Sommer to the defendant bank on April 16, 1929, and that on said 16th day of April 1929 the said defendant bank, acting by and through T. W. Mott, its cashier, issued its certificates of deposit to Frank F. Riese, who was then vice president of said defendant bank, one of said certificates a copy of which is hereto attached and made a part of this stipulation and marked Plaintiff's Exhibit Number Five, is numbered 116,081, in the sum of One Thousand Dollars, and that the other said certificate of deposit a copy of which is hereto attached and made a part of this stipulation and marked Plaintiff's Exhibit Number Six, is numbered 116,082, in the sum of

$58.98; that on the lower left-hand corner of each of said certificates of deposit is written in the handwriting of T. W. Mott, cashier of said defendant bank, in lead pencil, the words "W. C. Sommer"; that said Frank F. Riese departed this life in the year 1931, and that in the year 1932 by order of the County Court of Tazewell County, Illinois, the executors of the last will and testament of said Frank F. Riese endorsed both of said certificates to the order of the respondent Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, copy of which said endorsements appear on the backs of said Plaintiff's Exhibits Five and Six; that on the 15th day of April 1929 the credit balance of the defendant bank with the said First National Bank [fol. 55] of Peoria was $34,118.13; that said credit balance on each of the following dates was as follows:

1929	
April 16	$36,198.30
17	28,484.14
18	29,706.30
19	33,504.78
20	32,545.69
22	29,452.36
23	30,036.66
24	30,298.49
25	25,853.19

that on the 15th day of April 1929 the credit balance of the defendant bank with the said Merchants & Illinois National Bank of Peoria, Illinois, was $13,627.41; that said credit balance on each of the following dates was as follows:

1929	
April 16	$16,440.65
17	15,792.13
18	13,878.34
19	12,843.88
20	8,816.70
22	15,665.84
23	12,025.26
24	11,850.90
25	16,042.32

That the amount of cash on hand in said defendant bank at the time it was suspended on the 7th day of January 1932 was the sum of $26,235.10;

That on the 27th day of March 1929, said W. C. Sommer had to his credit in the Farmers National Bank of Pekin in the "Interest Account of W. C. Sommer" the sum of $192.50; that on the said 27th day of March 1929 there was credited to said Interest Account of W. C. Sommer the sum of $14,05.60, being a check drawn by one T. M. Smith on said Farmers National Bank of Pekin, Illinois, and payable to said Farmers National Bank; that said T. N. Smith was a lawyer and loan broker in the City of Pekin, Illinois, in the month of March 1929 and that in said month the said Sommer made arrangements with the said Smith to refinance a loan on the property of the said Sommer, of which the One Thousand Dollar note in question, dated November 1, 1923, due March 1, 1929 was a part; that on March 27, 1929 said Smith for the purpose of creating a fund to re-[fol. 56] finance said loan, made a deposit in said defendant bank of the sum of $14,308.10, said deposit being made up of checks and items as follows:

(Mr. Velde: Attorney for respondent is willing to stipulate as to the sources of the credit in the Farmers National Bank which enabled T. N. Smith to issue the check for $14,-055.60, but contends that the sources of that deposit are entirely irrelevant and immaterial in this case.)

check of W. C. Sommer on his interest account in the defendant bank in the sum of $55.60; check of Rev. H. C. Witte for the sum of $2,000.00, the bank upon which same was drawn and the place where said defendant bank deposited said check being unknown; check of N. H. Lee for the sum of $1500.00 on the Hoopeston National Bank, Hoopeston, Illinois, which said check was deposited by the said defendant bank in the Merchants & Illinois National Bank, Peoria, Illinois, on March 27, 1929, for credit; check of N. H. Lee for the sum of $1,000.00 drawn on the First National Bank of Hoopeston, Illinois, which check was deposited by the defendant bank for credit on March 27, 1929 in the First National Bank, Peoria, Illinois; check of Sarah Ubben for $1,050.00 drawn on the Herget National Bank of Pekin, Illinois; check of U. A. Ubben for the sum of $1,-680.00, drawn on the Herget National Bank of Pekin, Illinois; check of Theo. H. Ubben for the sum of $3,500.00 drawn on the Herget National Bank of Pekin, Illinois; that the said Ubben checks of $1,050.00, $1,680.00 and $3,500.00

were cleared between the Herget National Bank and the defendant bank on the 27th day of March 1929, the amount of the checks which the Farmers National Bank held on the Herget National Bank being $10,018.96 and the amount of the checks which the Herget National Bank held on the Farmers National Bank being $5,216.38, leaving a balance in favor of the Farmers National Bank of $4,802.58 which said balance amount of $4,802.58 the defendant bank on the said 27th day of March 1929 deposited for credit in the First National Bank of Peoria, Illinois; that another item of said T. N. Smith deposit consisted of "Sommer 10 interest coupons" in the amount of $467.50, which interest coupons were charged to the interest account of said W. C. Sommer in the said bank on March 27, 1929; that another item of the said T. N. Smith deposit is a check drawn by Fred Schreiber for the sum of one thousand dollars; that another of said items is a check drawn by Henry Schreiber [fol. 57] for $600.00; that another of said items is a check drawn by Anna M. Schreiber for $400.00; that another of said items is a check drawn by Sarah Ubben for $1,055.00; that as to the four last-mentioned checks it is not known on what bank or banks said checks were drawn, nor is it known where the funds derived by said defendant bank as the proceeds of such four checks were deposited by said defendant bank; that at the close of business on March 27, 1929 there was to the credit of said interest account of said W. C. Sommer in said Farmers National Bank the sum of $14,248.10; that thereafter on April 16, 1929 said W. C. Sommer paid to said Farmers National Bank the sum of $1,058.98 which amount was charged to the interest account of said W. C. Sommer, and that said sum of $1,058.98 is represented by said Plaintiff's Exhibits Five and Six above mentioned:

That on March 27, 1929 the credit balance of the defendant bank with the said Merchants & Illinois National Bank of Peoria, Illinois, was $14,442.50; that said credit balance on each of the following dates was as follows:

1929		
March	28	$16,936.24
	29	20,359.48
	30	19,492.37
April	1	20,077.04
	2	18,587.60
	3	18,105.61

4		16,344.60
5		14,394.95
6		12,169.63

That the credit balance of the defendant bank in the First National Bank of Peoria, Illinois, on March 27, 1929, was $46,096.79; that said credit balance on each of the following dates was as follows:

1929		
March	28	$38,027.31
	29	35,436.71
	30	33,325.18
April	1	26,872.51
	2	17,865.45
	3	23,133.41
	4	30,405.64
	5	29,073.45
	6	39,997.58

[fol. 58] That Plaintiff's Exhibit Number which is hereto attached and made a part of this stipulation is a true and correct copy of the check of said T. N. Smith referred to above, in the sum of $14.055.60;

That the five First Mortgage bonds of Elmer V. Veesaert and Emma M. Veesaert, Nos. 8452, 8456, 8457, 8458 and 8459, in the face amount of One Thousand Dollars each, which are referred to on page 4 of said decree, were involved in a foreclosure proceeding entitled Kirehert v. Veesaert, in the Circuit Court of Madison County, Illinois, and that the defendant Farmers National Bank as a holder of said five first mortgage bonds was made a party defendant in said cause; that the lands securing said notes and other notes of that series were sold by M. E. Newell, Master in Chancery of said Circuit Court of Madison County, at Edwardsville, Illinois, and that the proceeds of said fine notes which were then held by the defendant bank amounted to the sum of $1,597.31; that the said Master in Chancery on or about the 11th day of December 1930 remitted to the said Farmers National Bank of Pekin for its said distributive share in the sum of $1,597.31, by his check on the Edwardsville National Bank and Trust Company, payable to the Farmers National Bank of Pekin; that the said defendant bank immediately sent said check to the Edwardsville

National Bank and Trust Company for collection; that said Edwardsville National Bank and Trust Company sent to said defendant bank their draft No. 4,277 in the sum of $1,597.31, in payment of said check, said draft No. 4,277 being drawn on the Continental Illinois Bank and Trust Company, of Chicago, Illinois; that on December 13, 1930 the defendant bank sent said last-mentioned draft No. 4,277 for deposit and credit to the First National Bank of Chicago; that on December 13, 1930 the defendant bank issued its certificate of deposit, No. 118,763, payable to the Farmers National Bank, for $1,597.31, copy of which said certificate of deposit is hereto attached, marked Plaintiff's Exhibit Eight, and made a part of this Stipulation; that the original certificate of Deposit No. 118,763 bears the name "Veesaert" in the lower left-hand corner thereof in the handwriting of T. W. Mott, cashier of said defendant bank, who signed said certificate of deposit;

That the originals of said certificates of deposit copies of which are marked Plaintiff's Exhibits Two, Three, Four, Five, Six and Eight remained in the possession of the [fol. 59] said defendant bank from the dates of the issuance thereof down to the time of the appointment of Ross C. Adams as receiver of said defendant bank on the 26th day of January 1932, and that the said receiver has since been in possession thereof;

That the credit balance of the defendant bank in the First National Bank of Chicago, Illinois, on December 12, 1930, was $21,845.69; that said credit balance on each of the following dates was as follows:

1930	
December 13	$29,341.84
15	27,046.72
16	15,683.60
17	23,925.89
18	29,554.07
19	30,627.37
20	25,571.86
22	14,052.07
23	5,139.05

That the total credit balance of said Farmers National Bank with the First National Bank of Chicago on October 27, 1931, was $643.24;

(Mr. Covey: Plaintiff is willing to stipulate this fact but is quite sure that the same is wholly immaterial and irrelevant.)

It is further stipulated that at the close of business on January 7, 1932 by the Farmers National Bank of Pekin, that being the last day on which that bank was open for business, the credit balance of said Farmers National Bank with the First National Bank of Chicago, as shown by the books of the Farmers National Bank, was $10,827.03; and that soon thereafter the First National Bank of Chicago advised the respondent receiver that it, the First National Bank of Chicago, had appropriated and applied said entire balance on bills payable by the Farmers National Bank of Pekin to the First National Bank of Chicago, in the principal sum of $75,000.00; that the said bills payable of the defendant bank which were held by the First National Bank of Chicago aggregated the principal sum of $775,000 and were secured by diversified collateral consisting of utilities, industrial, domestic and foreign bonds of the approximate face value of $264,000.00; that on January 7, 1932 the approximate fair cash market value of such bonds was the [fol. 60] sum of $130,000.00; that after the First National Bank of Chicago had applied on the said bills payable of the Farmers National Bank the credit balance of the Farmers National Bank with said First National Bank of Chicago on January 7, 1932, the respondent Ross C. Adams as Receiver of said defendant bank paid off the balance still due on said bills payable to the First National Bank of Chicago, which balance approximated the sum of $53,000.00, whereupon the said collateral held by the First National Bank of Chicago was turned over and delivered to the respondent Ross C. Adams as such Receiver; that said collateral at the time said Receiver received same from the said First National Bank of Chicago was of the approximate fair cash market value of $110,000.00;

It Is Further Hereby Stipulated And Agreed by and between the parties hereto that this cause may be submitted to the Court and decided by it upon the records of this Court heretofore referred to and this stipulation, together with the exhibits attached thereto;

It Is Further Stipulated And Agreed by and between the parties hereto that this stipulation shall be written out by the court reporter and forwarded to the attorney for

the plaintiff, who shall prepare his written statement, brief and argument for the Court within ten (10) days from the date of the receipt of said stipulation; that plaintiff's attorney shall then furnish to respondent's attorney a copy of such brief and argument, and that the attorney for the respondent shall then reply thereto within ten (10) days after receipt thereof and shall furnish plaintiff's attorney with a copy thereof; that plaintiff's attorney shall then have five (5) days in which to reply to the brief of respondent's attorney.

It Is Further Hereby Stipulated And Agreed by and between the parties hereto that if the attorneys for the parties hereto, or either of them, desire to argue this case orally after the filing of such briefs, and if the Court be willing to listen to such argument, a short oral argument may be made at such time and place as the Court may fix.

(Which were all of the proceedings had in the above entitled cause on said day.)

L. M. James, Court Reporter, Springfield, Ill.

[File endorsement omitted.]

[fol. 61] PLAINTIFF'S EXHIBIT #1 L. M. J. 12/1/32

Department of Justice

United States District Court, Office of the Clerk, Southern District of Illinois

10/4/32.

Statement of Costs

In the matter of Edwin V. Champion, Trustee, v. The Farmers National Bank of Pekin, Illinois. No. 779, Equity.

Costs in the above cause to be paid by Defendant as directed in the Final Decree, as follows:

Clerk's fees	$ 16.35
Docket fee	20.00
Marshal's fees	2.60
Master's fees (First Report)	835.00
Reporter's fees " "	160.85
Master's fee (Second Report)	570.00
Reporter's fees " "	25.00
Total	$1629.80

I hereby certify that the above is a true and correct statement of the costs due in the above cause as shown by the files in the case.

S. T. Burnett, Clerk, U. S. District Court. (Seal.)

PLAINTIFF'S EXHIBIT #2. L. M. J. 12/1/32

(Copy)

70-230

The Farmers National Bank

115504

Pekin, Ill., Feb. 9, 1929. No. [120778]*

Farmers National Bank has deposited with this Bank payable to the order of same Exactly Three Thousand Dollars and No Cents. Dollars $3,000.00
on return of this Certificate properly endorsed.
10 shares Fitzgerald Bank Stock.
Certificate of Deposit.
Not subject to Check.

T. W. Mott, Cashier.

[fol. 62] PLAINTIFF'S EXHIBIT #3. L. M. J. 12/1/32

(Copy)

70-230

The Farmers National Bank

116062

Pekin, Ill. Apr. 12, 1929. No. [120782]*

Frank F. Riese has deposited with this Bank payable to the order of self Exactly Three Thousand Dollars $3,000.00
on return of this Certificate properly endorsed.
Chas. Graff.
Certificate of Deposit.
Not subject to Check.

T. W. Mott, Cashier.

---

* Figures in brackets erased in copy.

PLAINTIFF'S EXHIBIT #4. L. M. J. 12/1/34

(Copy)

70-230

The Farmers National Bank

116063

Pekin, Ill., Apr. 12, 1929. No. [120781]*

Frank F. Riese has deposited with this Bank payable to the order of self Exactly One Hundred, Eighty-three Dollars & 78/100 Dollars. $183.78.
on return of this Certificate properly endorsed.
Chas. Graff.
Certificate of Deposit.
Not subject to Check.

T. W. Mott, Cashier.

PLAINTIFF'S EXHIBIT #5. L. M. J. 12/1/32

(Copy)

70-230

The Farmers National Bank

116081

Pekin, Ill. Apr. 16, 1929. No. [120785]*

Frank F. Riese has deposited with this Bank payable to the order of self Exactly One Thousand Dollars No Cents.
[fol. 63] Dollars $1,000.00
on return of this Certificate properly endorsed.
W. C. Sommer.
Certificate of Deposit.
Not subject to Check.

T. W. Mott, Cashier.

---

* Figures in brackets erased in copy.

PLAINTIFF'S EXHIBIT #6. L. M. J. 12/1/32

(Copy)

70-230

The Farmers National Bank

116082

Pekin, Ill., Apr. 16, 1929. No. [120786]*

Frank F. Riese has deposited with this Bank payable to the order of self Exactly Fifty-eight Dollars Ninety-eight cents. Dollars $58.98
on return of this Certificate properly endorsed.
W. C. Sommer.
Certificate of Deposit.
Not subject to Check.

T. W. Mott, Cashier.

PLAINTIFF'S EXHIBIT #8. L. M. J. 12/1/32

(Copy)

70-230

The Farmers National Bank

118763

Pekin, Ill., Dec. 13, 1930. No. [120788]*

Farmers National Bank has deposited with this Bank payable to the order of same Exactly One Thousand Five Hundred Ninety-seven Dollars and 31/100. Dollars $1,597.31
n return of this Certificate properly endorsed.
Veesaert.
Certificate of Deposit.
Not subject to Check.

T. W. Mott, Cashier.

---

* Figures in brackets erased in copy.

[fol. 64] PLAINTIFF'S EXHIBIT #7. L. M. J. 12/1/32

(Copy)

70-230

Pekin, Illinois, March 27-1929. No. —

The Farmers National Bank

Pay to the order of Farmers Natl. Bank, Pekin, Ill., $14055.60/100 Fourteen Thousand fifty five & 60/100 Dollars for W. C. Sommer
Prin. $14000.
Int. to date $55.60.

T. N. Smith.

The following endorsements appear on backs of foregoing Exhibits, to wit:

Pl. Ex #3.
L. M. J.
12/1/32.

Pay to the Order of Ross C. Adams, Receiver, The Farmers National Bank, Pekin, Ill., without recourse.

(Signed) D. F. Lawley, (Signed) T. W. Mott, Executors of the Last Will & Testament of Frank F. Riese, deceased; as directed by court order in the County Court of Tazewell County, Illinois, July 5, 1932.

Pl. Ex #4.
L. M. J.
12/1/34.

Pay to the order of Ross C. Adams, Receiver, The Farmers National Bank, Pekin, Illinois, without recourse.

(Signed) D. F. Lawley, (Signed) T. W. Mott, Executors of the Last Will & Testament of Frank F. Riese, deceased: as directed by court order in the County Court of Tazewell County, Illinois, July 5, 1932.

Pl Ex #5.
L. M. J.
12/1/32.

[fol. 65] Pay to the order of Ross C. Adams, Receiver, The Farmers National Bank, Pekin, Illinois, without recourse.

(Signed) D. F. Lawley, (Signed) T. W. Mott, Executors of the Last Will & Testament of Frank F. Riese, Deceased; as Directed by Court Order in the County Court of Tazewell County, Illinois, July 5, 1932.

Pl. Ex. #6.
L. M. J.
12/1/32.

Pay to the order of Ross C. Adams, Receiver, The Farmers National Bank, Pekin, Illinois, without recourse.

(Signed) D. F. Lawley, (Signed) T. W. Mott, Executors of the Last Will & Testament of Frank F. Riese, Deceased; as Directed by Court Order in the County Court of Tazewell County, Illinois, July 5, 1932.

Pl. Ex. #7.
L. M. J.
12/1/32.

Cancelled paid March 27, 1929 by Farmers National Bank, Peoria, Ill.

IN UNITED STATES DISTRICT COURT

ORDER TAKING PETITION UNDER ADVISEMENT—Entered Jan. 12, 1933

Come the parties to this cause by Messrs. Covey, Covey & Covey and Messrs. Velde & Prettyman, their respective [fol. 66] attorneys, and this cause having come on for hearing on petition and answer filed herein, and after hearing the arguments of the respective attorneys and now being fully advised in the premises, the court takes the same under advisement.

IN UNITED STATES DISTRICT COURT

(Caption)

FINDINGS OF FACT AND HOLDING OF COURT—Filed June 30, 1933

This cause coming on to be heard upon the answer of the Receiver of The Farmers National Bank of Pekin, Illinois, reciting that he had complied with the final decree heretofore made and entered by this Court on the 24th day of June, 1932, with the exception of four items, in the aggregate of $8,870.07.

In the original cause the Trustee in Bankruptcy sued The Farmers National Bank of Pekin, Illinois, to recover an unlawful and recoverable preference which it had procured from John Fitzgerald on September 7, 1928, through the transfer to the bank of certain notes, bonds, bank stock, etc. of the face value of $26,000, which was deposited by the bankrupt with defendant as collateral security for a debt of the bankrupt in the sum of $26,000.

Upon the issues being made up the cause was referred to a Special Master, who found that the transfer of the said collateral security to said bank was null and void and should be set aside. On June 24, 1932, the said report of the Special Master was approved by the Court and final decree entered, ordering the bank to turn over and deliver to the plaintiff said notes, bonds and stock received by the bank from the bankrupt by way of an unlawful and recoverable preference. Defendant was ordered to pay to plaintiff $7,272.76, the value of a part of said personal property received by defendant from the bankrupt, which property the defendant had since its receipt collected or otherwise converted into cash, as follows:

Amount collected by defendant bank on Charles Graff note, April 12, 1929, principal and interest	$3,183.78
[fol. 67] Amount collected by defendant bank from W. C. Sommer note, April 16, 1929, principal and interest	$1,058.98
Amount received by defendant bank from sale of Ten (10) Shares of John Fitzgerald's Stock in defendant Bank, February 9, 1929, together with 3% dividend thereon	$3,030.00

The defendant was ordered in and by said decree to pay the sum of $7,272.76, at 5% interest from July 20, 1929, the date of the filing of the bill, to June 17, 1932, amounting to the sum of $1032.04, and directed the defendant to pay the costs of the proceeding to be taxed by the Clerk of the Court. Upon being taxed the costs amounted to $1629.80.

In the decree the Court found that in January, 1932, the defendant bank had been closed by the Comptroller of the Currency, and that Respondent Ross C. Adams had been appointed Receiver of the said bank by the Comptroller; and the Court ordered that the Comptroller and the Receiver perform all of the foregoing decree to be performed by the defendant bank, and they forthwith delivered to the plaintiff the said notes, and bonds which the Court had ordered the said defendant bank to turn over and deliver to plaintiff and that said Comptroller make the aforesaid payments to the plaintiff herein in due course of the administration of the affairs of said defendant bank. Jurisdiction was retained by the Court for further proceedings incident to the execution of the decree.

On August 26, 1932, a stipulation was entered into between the Trustee and the Receiver by which the said Receiver agreed to turn over and deliver to the plaintiff all of the notes, bonds, stock, etc., which had been received by the defendant bank from John Fitzgerald by way of unlawful or recoverable preference, except four items of the aggregate cash value of $8870.07, which were to be submitted to the Court.

(1) The Court finds that these four items are those above set forth which aggregate the principal sum of $8870.07.

(2) The Court further finds that the bank of the Receiver received the four items of collateral above described as an unlawful and recoverable preference; that the several elements were converted into cash and used by the Receiver's bank as its own.

(3) The Court further finds that the said several items [fol. 68] are and were impressed with a trust for the benefit of the creditors of John Fitzgerald, Bankrupt.

(4) The Court further finds that shortly after receiving the collaterals in question the defendant bank converted them into cash and treated them as such and as its own.

(5) The Court further finds that on January 7, 1932, when the said defendant bank closed, it had on hand in cash and cash items $36,054.76, and that this fund afterwards went into the hands of the Receiver; that the least amount in cash and cash items in the defendant bank during the period February 5, 1929, to the close of business on January 7, 1932, was $30,548.61; that the defendant bank by collecting notes and bonds belonging to the plaintiff as Trustee in Bankruptcy, and the sale of ten shares of stock, without the knowledge or consent of the Trustee, held the proceeds of such collections and sale, amounting to $8870.07, as a trustee ex maleficio, and that the said funds were in the funds on hand at the time of the closing of the bank, and that plaintiff is entitled to have said claim for $8870.07 allowed as a priority.

(6) The Court further finds that the plaintiff is entitled to have the costs in the sum of $1629.80 allowed as an ordinary claim against the receivership.

(7) The Court further finds that insofar as the general distribution of the Receiver fails to pay the amount of court costs heretofore taxed in this cause, that the balance is a proper charge against the recovery.

(8) The Court further finds that plaintiff is entitled to recover interest at the rate of 5% per annum on $7272.76, the amount received by the bank from the date of the bringing of the original suit, July 20, 1929, down to the date of the suspension of the bank, January 7, 1932, in the sum of $895.95. To this sum shall be added interest at 5% per annum on the amount collected from the Veesart notes by the defendant bank on December 13, 1930, on $1597.31, to the date of the suspension of the defendant bank, in the sum of $85.19, making a total amount of said interest which should be allowed as an ordinary claim of $991.14.

(9) The Court finds that as to the four items above referred to, the equities are with the plaintiff.

The Court holds, as a matter of law, that the plaintiff is entitled to recover of and from the Receiver the proceeds of the several notes and of the bank stock which the Bank had received as an unlawful preference, as a creditor of [fol. 69] John Fitzgerald, the bankrupt, and which said proceeds had been intermingled with the cash of the bank and treated as its own.

The plaintiff is entitled to an order granting it the relief sought herein, in harmony with the findings of fact and holdings herein made by the Court.

FitzHenry.

[File endorsement omitted.]

IN UNITED STATES DISTRICT COURT

(Caption)

DECREE—Filed July 7, 1933

The Court having heretofore, on the 30th day of June, 1933, filed in this cause its findings of fact and holdings of law, and directed that an Order be prepared in accordance therewith:

It Is, Therefore, Ordered, Adjudged and Decreed by the Court that the claim of the plaintiff herein, covered by the four items as follows:

1—Amount collected by defendant bank on Charles Graff note, April 12, 1929, principal and interest	$3,183.78
2—Amount collected by defendant bank from W. C. Sommer note, April 16, 1929, principal and interest	$1,058.96
3—Amount received by defendant bank from sale of Ten (10) Shares of John FitzGerald's Stock in defendant bank, February 9, 1929, together with 3% dividend thereon	$3,030.00
4—Proceeds of Veesaert Bonds received by defendant bank on or about December 13, 1930	$1,597.31

aggregating the sum of Eight Thousand Eight Hundred Seventy Dollars and Seven Cents ($8,870.07), be, and the same is hereby, allowed as a priority claim, to be paid in full; that the claim of said plaintiff for interest on said four (4) items, amounting to the sum of Nine Hundred Ninety One Dollars and Fourteen Cents ($991.14) be, and the same is hereby, allowed, as an ordinary claim; that the [fol. 70] court costs incurred in said original proceeding, amounting to the sum of Sixteen Hundred Twenty Nine

Dollars and Eighty Cents ($1629.80) be, and the same is hereby, allowed, as an ordinary claim.

It Is Further Ordered by the Court that the costs of this proceeding since the filing of the Plaintiff's petition on August 30, 1932, be taxed by the Clerk of this Court, including the costs of L. M. James, Court Reporter of this Court, for the preparation of the Stipulation entered into between the parties hereto on December 1st, 1932, and that such costs be allowed herein as a priority claim.

It Is Further Ordered by the Court that should other priority claims be allowed as against the said fund of Thirty Thousand Five Hundred Forty Eight Dollars and Sixty One Cents ($30,548.61), mentioned in Paragraph 5 of the Court's findings herein, in such sum or sums that the aggregate of all such priority claims against said fund should exceed the said sum of $30,548.61, then all priority claims allowed against said fund shall be pro-rated.

It Is Further Ordered by the Court that Ross C. Adams, Receiver of said defendant Bank, and the Comptroller of the Currency of the United States of America, be, and they are hereby, Ordered to perform this decree, and make the payments herein provided for, in accordance therewith, in the usual course of the administration of the affairs of said defendant Bank.

It Is Further Ordered that the Court retain jurisdiction of this cause for further proceedings incident to the execution of this decree.

To the entry of the foregoing decree, the defendant, The Farmers National Bank of Pekin, Illinois, and the respondent, Ross C. Adams, Receiver of said Farmers National Bank of Pekin, Illinois, except.

Louis FitzHenry, Judge.

[File endorsement omitted.]

[fol. 71] In United States District Court

Petition for Appeal—Filed Aug. 14, 1933

(Caption)

To the Hon. Louis FitzHenry, District Judge:

The above named defendant, Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, feeling

aggrieved by the decree rendered and entered in the above entitled cause on the 7th day of July, A. D. 1933, does hereby appeal from said decree to the United States Circuit Court of Appeals for the 7th Circuit for the reasons set forth in the assignment of errors filed herewith.

He shows to the court that he has been directed to pray this appeal by the Comptroller of the Currency of the United States; and he prays that his appeal be allowed without bond and that citation be issued as provided by law; and that a transcript of the record, proceedings and documents upon which said decree was based be duly authenticated and sent to the United States Circuit Court of Appeals for the 7th Circuit, under the rules of said court in such cases made and provided.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois. Franklin L. Velde and Wm. S. Prettyman, Attorneys for Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois.

Appeal allowed as prayed in the foregoing petition, without bond.

Aug. 14th, 1933.

[File endorsement omitted.]

IN UNITED STATES DISTRICT COURT

(Caption)

ASSIGNMENTS OF ERROR—Filed Aug. 14, 1933

The defendant, Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, in support of his attached petition and prayer for an appeal to the United States Circuit Court of Appeals for the 7th Circuit, assigns the following errors on the record herein, viz: that the learned District Judge erred in the following matters and respects, viz:

(1) In finding that the defendant, The Farmers National Bank of Pekin, Illinois was a trustee ex maleficio for the plaintiff herein.

[fol. 72] (2) In ordering and decreeing that the sum of eight thousand, eight hundred seventy dollars and seven ($8870.07) cents or any part thereof, be allowed as priority or preferred claim against this defendant and the assets of said bank.

(3) In not requiring proof that the assets of said bank were augmented by the payment of said sum of eight thousand, eight hundred seventy dollars and seven ($8870.07) cents or any part thereof.

(4) In not requiring the plaintiff to trace said sum of eight thousand, eight hundred seventy dollars and seven ($8870.07) cents into the hands of this defendant or into the assets received by him from said bank.

For the foregoing reasons, this defendant prays that the decree or order of the District Court entered herein on the 7th day of July, A. D. 1933 be reversed.

Respectfully submitted, Franklin L. Belde and Wm. S. Prettyman, Attorneys for Appellant, Ross C. Adams, Receiver of the Farmers' National Bank of Pekin, Illinois.

IN UNITED STATES DISTRICT COURT

AFFIDAVIT OF FRANKLIN L. VELDE—Filed Aug. 14, 1933

(Caption)

Franklin L. Velde being grst duly sworn deposes and says that he is one the attorneys for the defendant, Ross, C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois; that in pursuance to the suggestion of Hon. Louis FitzHenry, Judge of said court, this deponent on the 12th day of August, A. D. 1933, telephoned to I. J. Covey, attorney for the plaintiff in the above entitled cause and advised said Covey that this deponent expected to present on the 14th day of August, A. D. 1933 to said Judge Louis FitzHenry at the latter's chambers in the United States Court Building at Bloomington, Illinois, a prayer for an appeal by said defendant Adams as such receiver to the [fol. 73] United States Circuit Court of Appeals for the 7th Circuit from the decree entered herein on the 7th day

of July, A. D. 1933; and also an assignment of errors and advised said Covey that the notice was given so that said Covey might be present or take such other action in the matter as he, said Covey might deem advisable.

This deponent further says that said Attorney I. J. Covey then and there advised this deponent, that he, said Covey had no objection to the filing and presentation of such petition or prayer for an appeal, together with an assignment of errors; that he, said Covey would not be present and that he would not and did not require any further or other notice of the intention to present the prayer or petition for such appeal and said assignment of errors.

And further deponent sayeth not.

Franklin L. Velde.

STATE OF ILLINOIS,
County of Tazewell, ss:

Subscribed and sworn to before me this 14th day of August, A. D. 1933. Delia I. Morris, Notary Public. (Seal.)

[File endorsement omitted.]

IN UNITED STATES DISTRICT COURT

ORDER ALLOWING APPEAL—Entered Aug. 14, 1933

Appeal allowed as prayed in the foregoing petition, without bond.

[fol. 74] IN UNITED STATES DISTRICT COURT

ORDER EXTENDING TIME—Filed Sept. 12, 1933

(Caption)

This cause coming on this day to be heard upon the motion of the defendant herein, by its attorney for an extension of time within which to prepare and file the transcript of record herein, and for an enlargement of the return day of the Citation on Appeal heretofore issued herein, and the Court having heard and duly considered the same, it is,

Ordered that the time for preparing and filing the transcript of record herein be and is hereby extended for a period of thirty days from and after the 13th day of September, 1933, to and including the 12th day of October, 1933.

And it is further ordered by the court that the return day of the Citation on Appeal issued herein be and is hereby enlarged for a period of thirty days from and after the 13th day of September, 1933, to and including the 12th day of October, 1933.

FitzHenry, Judge.

[File endorsement omitted.]

[fol. 75] IN UNITED STATES DISTRICT COURT

PRÆCIPE FOR RECORD—Filed Aug. 21, 1933

(Caption)

To S. T. Burnett, Esq., Clerk of the District Court of the United States for the Southern District of Illinois:

In the above entitled case, which was conducted in your court as Equity Case No. 779, wherein Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt, was plaintiff and the Farmers National Bank of Pekin, Illinois, et als., were defendants, will you kindly prepare a transcript of the record for appeal, containing the following items, documents and proceedings, viz:

(1) Petition or complaint filed on July 20, 1929.

(2) Date of filing of answer of the defendant, the Farmers National Bank of Pekin, Illinois.

(3) Date of Order referring cause to special master-in-chancery.

(4) Date of filing of report of special master-in-chancery.

(5) Date of order of rereference to special master-in-chancery.

(6) Date of filing of second or amended report of special master-in-chancery.

(7) The following portions of the opinion of Judge FitzHenry filed in or about June 14, 1932, viz:—

(a) Pages 1 and 2 thereof.

(b) The last seven (7) lines on page 4 and the first five (5) lines on page 5.

(c) All of page 13 and all of the balance of said opinion.

(8) The order of Judge FitzHenry in support of his said opinion and overruling exceptions to the special master's reports.

(9) Decree entered by Judge FitzHenry on June 24, A. D., 1932.

(10) All orders, opinions of court, pleadings, stipulations and proceedings filed or entered in said cause, subsequent to June 24, 1932. No documents to appear in the record more than once.

Dated this 21st day of August, A. D., 1933.

Franklin L. Velde and Wm. S. Prettyman, Attorneys for Appellant Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois.

[File endorsement omitted.]

[fol. 76] Clerk's Certificate to foregoing transcript omitted in printing.

IN UNITED STATES DISTRICT COURT

(Caption)

WAIVER OF CITATION—Aug. 17, 1933

Now comes the appellee in the above entitled cause, by his duly authorized attorney and waives the issuance and service of citation in the above entitled case and enters his appearance therein.

Dated this 17th day of August, A. D. 1933.

Ira J. Covey, Attorney for Appellee.

[File endorsement omitted.]

UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

I, Frederick G. Campbell, Clerk of the United States Circuit Court of Appeals for the Seventh Circuit, do hereby certify that the foregoing printed pages, numbered from 1 to 76, inclusive, contain a true copy of the printed record, printed under my supervision and filed on the tenth day of November, 1933, and used and considered at the hearing and on the determination of the following entitled cause:

Ross C. Adams, Receiver of The Farmers National Bank,
Appellant,

vs.

Edwin V. Champion, Trustee in Bankruptcy, etc.,
Appellee,

No. 5076, October Term, 1933, as the same remains upon the files and records of the United States Circuit Court of Appeals for the Seventh Circuit.

In Testimony Whereof I hereunto subscribe my name and affix the seal of said United States Circuit Court of Appeals for the Seventh Circuit, at the City of Chicago, this 28th day of June, A. D. 1934.

FREDERICK G. CAMPBELL,
(Seal) *Clerk of the United States Circuit Court of Appeals for the Seventh Circuit.*

At a regular term of the United States Circuit Court of Appeals for the Seventh Circuit, begun and held in the United States Court Room in the City of Chicago, in said Seventh Circuit on the fourth day of October, 1932, of the October Term in the year of our Lord One Thousand Nine Hundred and Thirty-two and of our Independence the One Hundred and Fifty-seventh.

Ross C. Adams, Receiver of The Farmers National Bank of Pekin, Illinois,
5076 *vs.*
Edwin V. Champion, Trustee in Bankrupty of John FitzGerald, Bankrupt.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

And on, to-wit: On the twenty-ninth day of September, 1933, there was filed in the office of the Clerk of this court an appearance of the appellant, which said appearance is in the words and figures following, to-wit:

UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5076. October Term, 1933.

Ross C. Adams, Receiver, etc.,
Appellant,

vs.

Edwin V. Champion, Trustee, etc.,
Appellee.

The Clerk will enter my appearance as counsel for the appellant.

FRANKLIN L. VELDE,
WILLIAM S. PRETTYMAN,
Constituting firm of Velde & Prettyman,
Pekin, Illinois.

Endorsed: Filed September 29, 1933, Frederick G. Campbell, Clerk.

At a regular term of the United States Circuit Court of Appeals for the Seventh Circuit, begun and held in the United States Court room in the City of Chicago, in said Seventh Circuit on the fourth day of October, 1933, of the October Term in the year of our Lord One Thousand Nine Hundred and Thirty-three and of our Independence the One Hundred and Fifty-eighth.

And on the same day, to-wit: On the third day of October, 1933, there was filed in the office of the Clerk of this court an appearance of counsel for appellee, which said appearance is in the words and figures following, to-wit:

UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5076. October Term, 1933.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,

Appellant,

vs.

Edwin V. Champion, Trustee in Bankruptcy, etc.,

Appellee.

The Clerk will enter my appearance as counsel for the appellee.

IRA J. COVEY,
EDWIN L. COVEY,
Peoria, Ill.

Endorsed: Filed October 3, 1933, Frederick G. Campbell, Clerk.

And afterwards, to-wit: On the ninth day of January, 1934, the following further proceedings were had and entered of record, to-wit:

Tuesday, January 9, 1934.

Court met pursuant to adjournment and was opened by proclamation.
Before:

Hon. Samuel Alschuler, Circuit Judge.
Hon. Evan A. Evans, Circuit Judge.
Hon. William M. Sparks, Circuit Judge.

5076 Ross C. Adams, Receiver, etc. *vs.* Edwin V. Champion, Trustee. } Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

It is ordered by the court that this cause be, and the same is hereby set down for hearing on February 20, 1934.

And afterwards, to-wit: On the twentieth day of February, 1934, the following further proceedings were had and entered of record, to-wit:

Tuesday, February 20, 1934.

Court met pursuant to adjournment and was opened by proclamation.

Before:

Hon. Samuel Alschuler, Circuit Judge.
Hon. Evan A. Evans, Circuit Judge.
Hon. William M. Sparks, Circuit Judge.

5076 Ross C. Adams, Receiver, etc. *vs.* Edwin V. Champion, Trustee, etc. } Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

Now this day comt the parties by their counsel and this cause now comes on to be heard on the printed record and briefs of counsel and on oral arguments by Mr. Franklin L. Velde, counsel for appellant, and by Mr. Ira J. Covey, counsel for appellee, and the court having heard the same takes this matter under advisement.

And afterwards, to-wit: On the seventeenth day of April, 1934, there was filed in the office of the Clerk of this court the opinion of the court, which said opinion is in the words and figures following, to-wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5076. October Term, 1933, April Session, 1934.

ROSS C. ADAMS, Receiver of the Farmers National Bank of Pekin, Illinois,
Appellant,
vs.
EDWIN V. CHAMPION, Trustee in Bankruptcy of JOHN FITZGERALD, Bankrupt,
Appellee.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

April 17, 1934.

Before ALSCHULER, EVANS, and SPARKS, *Circuit Judges.*

This appeal involves the preference of appellee's claim against the receiver of the Farmers National Bank of Pekin, Illinois.

SPARKS, *Circuit Judge.* On September 7, 1928, John Fitzgerald deposited with the bank certain farm mortgage notes, and certificates for thirty shares of the bank's stock, as collateral security for his renewal note of that date in the amount of $26,000. On October 26, 1928, an involuntary proceeding in bankruptcy was filed against him, and on November 16, 1928, he was adjudged a bankrupt.

On July 20, 1929, appellee filed a bill against the bank to recover preferences made within four months immediately preceding the filing of the petition in bankruptcy which included the collateral pledged as security for Fitzgerald's note for $26,000. The answer filed by the bank is not in this rec-

ord, but from the court's memorandum opinion it is obvious that the issues were: (1) Did the bank at the time of the transfer have reasonable cause to believe that Fitzgerald was insolvent, and (2) did the bank still have in its possession any of the pledged collaterals or their proceeds. The matter was referred to a master who answered both questions in the affirmative, and found the issues for the trustee. The bank excepted to the findings, and the court sustained the master on June 17, 1932, and on June 24, entered a decree ordering the collaterals or their proceeds delivered to the trustee.

In the meantime on January 7, 1932, the bank had closed its doors, and on January 26, 1932, the Comptroller of the Currency had appointed appellant as its receiver. As a part of the decree it was ordered that a certified copy of it be sent by registered mail to the Comptroller, in which he was ordered on behalf of the bank to comply with the terms of the decree, and it is admitted that the letter was received by him. From this decree no appeal was prosecuted. Up to this time, so far as the record shows, neither the Comptroller nor the receiver had knowledge of this proceeding. This fact, however, would have no effect on the binding force of the decree upon him, *Bereth* v. *Sparks,* 51 F. (2d) 441, and he complied with its terms except as to the four following items of collateral which form the basis of this controversy:

Charles Graff mortgage note and interest	$3,183.78
W. C. Sommers " " " "	1,058.98
Ten shares of Farmers bank stock and dividend	3,030.00
Veesaert notes and interest	1,597.31.

On August 30, 1932, appellee filed his petition for an order requiring appellant to pay petitioner in cash the four items above referred to, on the grounds that the first two items had been paid to the bank in the early part of 1929, the third converted into cash about the same time and the last item had been paid on December 13, 1930, and that the receiver now held the entire amounts for the appellee as trustee *ex maleficio.* The issues were joined by appellant's answer in which he admitted the validity of appellee's claim as an unpreferred claim but denied the existence of a trust *ex maleficio;* or that the bank's assets, by any of these transactions had been augmented; or that any part of the funds demanded had been traced into his hands. All the facts were stipulated and it was therein agreed that either the trustee or the receiver might apply to the court for a decision and decree as to any matter in dispute. Upon submission the court made

findings of fact and rendered its conclusions of law favorable to appellee with respect to the four items in controversy. The court's findings which are material to the questions here presented are substantially as follows: That the bank received the four items of collateral as an unlawful and recoverable preference and treated them as cash and shortly thereafter converted them into cash which was intermingled with the cash of the bank and treated by it as its own; that when the bank closed it had on hand in cash and cash items, $36,054.76, which afterwards went into the hands of the receiver; that the least amount in cash and cash items in the bank during the period from February 5, 1929, to the close of the business on January 7, 1932, was $30,548.61; that the bank by collecting bankrupt's notes and bonds and by sale of his bank stock without the knowledge or consent of the trustee, held the proceeds of such collections and sale amounting to $8,870.07 as a trustee *ex maleficio;* and that said funds were in the possession of the bank when it closed.

When Fitzgerald's securities were pledged to the bank, it can not be doubted that the bank knew that he was insolvent, or by the exercise of ordinary diligence ought to have known it, and it is not denied that the other elements necessary to constitute a preference were present. These facts were determined by the first decree and were supported by substantial evidence. There was neither exception nor appeal with respect to that decree, and we do not understand that appellant in this proceeding is denying that there was an unlawful preference.

It is first contended by appellant that the court erred in finding that the bank was a trustee *ex maleficio* for the bankrupt. In his brief it is stated, "We do not admit there was a trust relationship nor do we confidently deny it." Counsel for appellee calls our attention to what he styles certain admissions with respect to the existence of a trust, made in appellant's brief in the District Court. That brief is not in this record and constitutes no part of it, and counsel should know that it should not be referred to in argument. It is quite obvious from the facts found, however, that some form of trust relationship existed between Fitzgerald and the bank and that it was a constructive trust relationship, due to the fact that the bank had wrongfully taken possession and assumed control of Fitzgerald's property. *Baltimore and Ohio Telephone Co.* v. *Interstate Telephone Co.,* 54 Fed. 50; *In re Maher,* 144 Fed. 503. We think the court properly held that

it was a trust *ex maleficio*. *Smith* v. *Mottley*, 150 Fed. 266; *Brennan* v. *Tillinghast*, 201 Fed. 609.

It is next contended by appellant that the bank's assets were not augmented by the amounts received by it in payment of the obligations of the collateral. That is no doubt true, but the assets of the bank had been previously augmented when it wrongfully took possession of the collateral obligations. At that time the trust attached, and the fact that the collateral obligations were subsequently liquidated would not destroy the trust, and it would make no difference whether the collateral obligations were paid from money in the appellant's bank or from any other source.

It is further contended by appellant that the property in controversy has not been traced into his possession, which of course is necessary before appellee can recover. In *Schumacher* v. *Harriet*, 52 F. (2d) 817, it was disclosed that plaintiff had delivered life insurance checks to the bank to purchase bonds for plaintiff with the proceeds; that the checks were received by the bank as cash and treated by it as such, plaintiff receiving immediate credit therefor; that it forwarded the checks for credit to correspondent banks, in which on that day, and for several days thereafter, the sending bank had credit balances considerably in excess of the respective amounts so deposited. Those balances were gradually reduced until, at the time of the depositing bank's failure, the account with one of the correspondent banks showed an overdraft, and the account with another bank showed a small balance which was credited upon a note which the correspondent bank held. It was there said that the plaintiff, under those circumstances, had traced the trust fund in the bank receiver's hands. The court said, "* * * where a bank acting as trustee mingles a trust fund with its other funds, the common fund resulting is impressed with a trust to the amount of the trust fund which has been so commingled and lost its identity; and in such case the *cestui que trust* is entitled to have the trust declared and the trust fund separated from the other funds, even though the bank subsequently to the commingling may have added to and made payments from the common fund, as the presumption is that it respected the trust and did not make payment from the trust property. A limitation upon the rule is that the amount for which the trust is declared may not exceed the smallest amount which the common fund contained subsequent to the commingling of the trust funds. *Central National Bank* v. *Conn. Mut. Life Ins.*

Co., 104 U. S. 54; *Poisson* v. *Williams*, 15 F. (2d) 582; *Brennan* v. *Tillinghast*, 201 Fed. 609; *Empire State Surety Co.* v. *Carroll*, 194 Fed. 593." Quoting from the opinion of Judge Sanford in *Brennan* v. *Tillinghast*, the court said, " 'It is undisputed that the proceeds of the sale of Brennan's stock, wrongfully converted by the Ironwood Bank to its own use, constituted a trust fund, which did not lose this character when mingled with other moneys of the bank, and that Brennan was entitled to recover the amount thereof as a preferred claim, if, and to the extent that, he sustained the burden of proof of tracing this money, either in its original shape or in a substituted form, into the moneys which came into the hands of the receiver as part of the assets of the bank. (Citing cases.) And proof that the tort-feasor has mingled the trust funds with his own and made payments thereafter out of the common fund, is, nothing else appearing, a sufficient identification of the remainder of that fund coming into the hands of the receiver, not exceeding the smallest amount the fund contained subsequent to the commingling, as trust property, under the legal presumption that he regarded the law and neither paid out the trust fund nor invested it in other property, but kept it sacred.' "

With respect to tracing the fund in the Schumacher case, the court said, "As the fund upon which the trust is asserted * * is the fund of cash and cash items which passed into the hands of the receiver, the question in the case is whether the $8,500 of plaintiff has been traced into that fund; * * We think that this question must be answered in the affirmative. The life insurance checks were received by the bank as cash and were treated by it as such. They increased the cash and cash items in the tills of the bank at the time. When it placed them to its credit in the Richmond and New York banks, it was dealing with them as its own; and the presumption is that cash which was left in its tills was intended to be subject to the trust. While it had, of course, the right to collect the checks, it had no right to place their proceeds to its credit in other banks without holding an equivalent amount in cash in its own vaults to satisfy the trust which it had assumed towards plaintiff; and we must assume that it respected the trust, as 'equity imputes an intention to fulfill an obligation.' "

The facts in the Schumacher case are quite analogous to those found by the court in the instant case, and a perusal of the evidence leaves no doubt in our minds that the court's

findings here are supported by substantial evidence. We are convinced that the bank's assets were augmented by, and to the extent of, the proceeds of the collateral, and that those proceeds have in law been traced into the receiver's hands.

It is no doubt true, as appellant insists, that the only preference expressly allowed by the Act of Congress in cases of insolvency of a national bank is the one to the United States for advances in redeeming notes of the bank, but that statute was never intended to, and does not, prevent a preference for trust funds. It is indeed doubtful if Congress could prevent such a preference if it so desired.

Decree affirmed.

And on the same day, to-wit: On the seventeenth day of April, 1934, the following further proceedings were had and entered of record, to-wit:

Tuesday, April 17, 1934.

Court met pursuant to adjournment and was opened by proclamation.

Before:

Hon. Samuel Alschuler, Circuit Judge.
Hon. Evan A. Evans, Circuit Judge.
Hon. William M. Sparks, Circuit Judge.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,
5076 *vs.*
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

This cause came on to be heard on the transcript of the record from the District Court of the United States for the Southern District of Illinois, Northern Division, and was argued by counsel.

On consideration whereof: It is now here ordered, adjudged and decreed by this court that the decree of the said District Court in this cause be, and the same is hereby affirmed with costs.

And afterwards, to-wit: on the fourth day of May, 1934, there was filed in the office of the Clerk of this court a motion to extend the time to file petition for rehearing, together with stipulation and agreement, affidavit of Ross C. Adams and affidavit of Jesse Black, Jr., which said motion, stipulation and affidavits are in the words and figures following, to-wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS,

For the Seventh Circuit.

No. 5076. OCTOBER TERM, 1933, APRIL SESSION, 1934.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,
Appellant,
vs.
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt,
Appellee.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

To the Honorable Presiding Judges of Said Court:

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, appellant in the above entitled cause, by Jesse Black, Jr., his attorney, moves the Court for an extension of time of fifteen (15) days after May 7, 1934 in which to file petition for re-hearing and in support of said motion submits the following:

1. Stipulation and consent signed by Ira J. Covey and Edwin L. Covey, attorneys for Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt, Appellee.
2. Affidavit of Ross C. Adams, Appellant.
3. Affidavit of Jesse Black, Jr.

Respectfully submitted,

ROSS C. ADAMS,
Receiver of Farmers National Bank, Pekin, Illinois, Appellant,
By JESSE BLACK, JR.,
His Attorney.

Granted 5-3-34.
WILLIAM M. SPARKS.

IN THE UNITED STATES CIRCUIT COURT OF APPEALS,

For the Seventh Circuit.

No. 5076. OCTOBER TERM, 1933, APRIL SESSION, 1934.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,
Appellant,
vs.
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt,
Appellee.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

STIPULATION AND AGREEMENT.

And now comes Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt, appellee, by Ira J. Covey and Edwin L. Covey, his attorneys, and as to the motion of appellant for an extension of time in which to file petition for re-hearing, state that they have read said motion and the supporting affidavits and that they have no objection, as attorneys for Appellee, to the granting of said extension of time in which to file petition for re-hearing prayed for by Appellant.

IRA J. COVEY,
EDWIN L. COVEY,
Attorneys for Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt, Appellee.

IN THE UNITED STATES CIRCUIT COURT OF APPEALS,

For the Seventh Circuit.

No. 5076. OCTOBER TERM, 1933, APRIL SESSION, 1934.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois.
Appellant,
vs.
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt.
Appellee.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

AFFIDAVIT.

ROSS C. ADAMS, Receiver of the Farmers National Bank of Pekin, Illinois and appellant in the above entitled cause, being first duly sworn upon his oath deposes and says that prior to the argument of this case orally before your Court the firm of Velde & Prettyman had been relieved as attorneys for the Receiver of the Farmers National Bank of Pekin, Illinois, by the Comptroller of the Currency and Judge Jesse Black, Jr., had been appointed to that position. Authority had been granted the firm of Velde & Prettyman to argue this cause but as soon as the opinion had been handed down the Comptroller of the Currency designated Judge Jesse Black, Jr., of Pekin, Illinois, to proceed with the conduct of said cause as will be hereafter shown in this affidavit.

Deponent further states that since December 19, 1933, the said firm of Velde & Prettyman have not been the attorneys for deponent as Receiver except in the above entitled cause and one or two other unfinished matters; that the present attorney for deponent as such Receiver is Judge Jesse Black, Jr., of Pekin, Illinois.

Deponent further states that the opinion of the Court in this cause was filed on April 17, 1934 and that deponent received a copy of the opinion from his former attorney, Mr. Franklin L. Velde, on April 20, 1934; that thereupon deponent immediately mailed a copy of the opinion to the Comptroller of the Currency of the United States at Washington, D. C.

with a request for instructions as to what further course to pursue; that on the morning of May 3, 1934 he received a special delivery letter from the Comptroller of the Currency directing him to have his present attorney, Judge Jesse Black, Jr., prepare and file in this Court in the above entitled cause a petition for re-hearing.

Deponent further states that he at once went to the office of his attorney, Judge Jesse Black, Jr., in the Farmers National Bank Building, Pekin, Illinois, and exhibited to him the said letter of instruction of the Comptroller of the Currency.

Deponent further states that his present counsel, Judge Jessee Black, Jr., did not try this cause in this Court or in the District Court of the United States; that he is informed by his said counsel that it will be physically impossible for him to make the necessary research, examination of the records, authorities and the opinion, prepare a petition for re-hearing, have it printed and filed by May 7, 1934, the date on which petition for re-hearing must be filed under the existing rules of this Court.

Deponent further states that on account of the extraordinary amount of business which the office of the Comptroller of the Currency has at the present time with closed banks and receiverships that said Comptroller's office was unavoidably delayed in getting the instructions to file petition for re-hearing to deponent.

Deponent further states that in the letter of the Comptroller of the Currency hereinbefore referred to and received by deponent on this day, the following language occurred:

> "We desire that Judge Black take over the handling of this case to the exclusion of Messrs. Velde & Prettyman, your former attorneys."

Deponent further states that this application for extension of time in which to file petition for re-hearing is not for delay but that justice may be done and that his present counsel may have adequate time in which to prepare said petition for re-hearing.

Further deponent saith not.

ROSS C. ADAMS,
Receiver of the Farmers National Bank of Pekin, Illinois, Appellant.

Subscribed and sworn to before me this 3rd day of May, A. D. 1934.

HESTER E. HOLLAND,
Notary Public.

(Seal)

IN THE UNITED STATES CIRCUIT COURT OF APPEALS,

For the Seventh Circuit.

No. 5076. OCTOBER TERM, 1933, APRIL SESSION, 1934.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,
Appellant,
vs.
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt,
Appellee.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

AFFIDAVIT.

JESSE BLACK, JR., being first duly sworn upon his oath, deposes and says that he is attorney for Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, appellant in the above entitled cause; that he has been such attorney since about the nineteenth day of December, 1933, but that when he became such attorney, by special authority granted by the Comptroller of the Currency the firm of Velde & Prettyman were to conclude all proceedings relating to the trial of the above entitled cause; that since said time the relations and connections of Velde & Prettyman have been terminated by the Comptroller of the Currency.

Deponent further states that on this day, May 3, 1934, Mr. Ross C. Adams, Receiver, appellant in the above entitled cause, came to deponent's office with a letter from the Comptroller of the Currency containing instructions to deponent to prepare and file in this Court a petition for re-hearing in the above entitled cause.

Deponent further states that under the rule of this Court said petition must be filed on May 7, 1934; that to prepare a petition for re-hearing properly and in a lawyer-like way will require an examination of all the Briefs on both sides of the case, the record in the case, and the authorities; that de-

ponent did not try this cause either in the District Court of the United States or in this Circuit Court of Appeals and that it is physically impossible for him to do the necessary research and examination and properly prepare and have printed the petition for rehearing by May 7, 1934.

Deponent further states that the motion for extension of time is not made for delay but that justice may be done.

Further deponent saith not.

JESSE BLACK, JR.,
Attorney for Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, Appellant.

Subscribed and sworn to before me this 3rd day of May, A. D. 1934.

(Seal)

HESTER E. HOLLAND,
Notary Public.

(Endorsed) Filed May 4, 1934. Frederick G. Campbell, Clerk.

And on the same day, to-wit: On the fourth day of May, 1934, the following further proceedings were had and entered of record, to-wit:

Friday, May 4, 1934.

Court met pursuant to adjournment and was opened by proclamation.

Before:

Hon. Samuel Alschuler, Circuit Judge.
Hon. William M. Sparks, Circuit Judge.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,
5076 *vs.*
Edwin V. Champion, Trustee, etc.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

On motion of counsel for appellant, counsel for appellee not objecting, it is now here ordered that the time to file a petition for a rehearing in this cause be, and the same is hereby extended 15 days after May 7, 1934.

And afterwards, to-wit: On the seventeenth day of May, 1934, there was filed in the office of the Clerk of this court a petition for rehearing, which said petition for rehearing is in the words and figures following, to-wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

October Term, A. D. 1933.

April Session, 1934.

No. 5076.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,
Appellant-Petitioner,
vs.
Edwin V. Champion, Trustee in Bankruptcy, of John Fitzgerald, Bankrupt,
Appellee-Respondent.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

Honorable
Louis FitzHenry,
Trial Judge.

APPELLANT'S PETITION FOR REHEARING.

Counsel for Appellant:

JESSE BLACK, JR.,
Farmer's Nat'l Bank Bldg.,
Pekin, Illinois,
JOHN F. ANDERSON,
Care Comptroller of the Currency,
Washington, D. C.

Counsel for Appellee:

IRA J. COVEY,
Jefferson Building,
Peoria, Illinois,
EDWIN L. COVEY,
Jefferson Building,
Peoria, Illinois,

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Statement of Facts *1

Summary of Argument.

A. History of the decision in Schumacher v. Harriet, 52 Fed. (2nd) 817, was not fully presented to the Court. The instant case has no class aspect except on the question of tracing funds. Petition for rehearing directed to this feature exclusively. The Comptroller of Currency is now engaged in winding up 1,540 insolvent National banks through Receivers, many located in the Seventh Circuit. The National Bank Act contemplates a liquidation that will be uniform throughout the States 2

A preferred claim against an insolvent National Bank cannot be established in the absence of affirmative proof and especially proof of tracing funds to the Receiver. Claimant has the burden of identifying the property in its original or later form. The decision in Schumacher v. Harriet relied upon by this Court is out of line with the decisions of the Supreme Court of the United States and all other Circuit Courts of Appeal. The tracing of funds principle applied by this Court in this case is a variance with the holdings of other Circuit Courts of Appeal giving a distinct class aspect to this case important to the Comptroller of the Currency in the liquidation of insolvent banks..... 2

B. The contention of the Receiver on rehearing is that on the record all claims based upon any items are general only except as to the extent of $643.23, the Veesaert item, because of the inability of claimant to affirmatively trace proceeds in excess of this amount into the hands of the Receiver, said items being as follows:

Charles Graff mortgage note and interest	$3,183.78
W. C. Sommer mortgage note and interest	1,058.98
Ten shares, Farmers bank stock and dividend	3,030.00
Veesaert notes and interest.....	1,597.31

* Small figures in parentheses show commencement of original page.

The relationship created by the general deposits in each of the above cases was that of debtor and creditor and not that of trustee and cestui que trust..... 4

C. The principle announced as to the tracing of funds in Schumacher v. Harriet, 52 Fed. (2nd) 817 is unsound; it is at variance with the holdings of every other Circuit Court of Appeal called upon to decide the question and the Schumacher case has been rejected by every other Circuit Court of Appeal when brought to such Court's attention. The doctrine in Schumacher v. Harriet has been rejected in principle by the Supreme Court of the United States. Further, the tracing of funds principle of the Schumacher v. Harriet case is not applicable to this case at the bar of this Court.... 10

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IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

October Term, A. D. 1933.

April Session, 1934.

No. 5076

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,
Appellant-Petitioner,
vs.
Edwin V. Champion, Trustee in Bankruptcy, of John Fitzgerald, Bankrupt,
Appellee-Respondent.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.
Honorable
Louis FitzHenry,
Trial Judge.

APPELLANT'S PETITION FOR REHEARING.

To the Honorable Presiding Judges of said Court:

Ross C. Adams, receiver of the Farmers National Bank of Pekin, Illinois, appellant and petitioner herein, respectfully submits that he desires to make the following suggestions to this court in support of his petition for rehearing.

(2)

Interest of the Comptroller of the Currency in the Case.

(A) When the opinion of the court in this case, dated April 17, 1934, came to the attention of the Comptroller of the Currency he immediately directed his agent, the Receiver of the Farmers National Bank of Pekin, Illinois, to file a petition for rehearing on the theory that the rather voluminous record in the case made it quite difficult to segregate the pertinent facts concerning tracing of funds to the receiver and that the history of the decision in *Schumacher* v. *Harriet,* 52 Fed.

(2nd) 817 was not fully presented to the court. The case has no class aspect except on the question of tracing of funds, hence the petition for rehearing is directed to this feature exclusively.

The Comptroller of the Currency is now engaged in the winding up of 1,540 insolvent national banks through receivers appointed by him and many of these banks are located in the Seventh Circuit.* The National Bank Act, a code by itself for the winding up of such banks, contemplates a liquidation that will be uniform throughout the 48 States. *Cook County National Bank* v. *United States*, 107 U. S. 445; *First National Bank* v. *Selden*, 120 Fed. 212; *Davis* v. *Elmira Savings Bank*, 161 U. S. 275; *Easton* v. *Iowa*, 188 U. S. 220. Neither the United States, a state or its political subdivisions nor an individual can establish a preferred claim against an insolvent national bank in the absence of affirmative proof of the three essentials of trust relationship, augmentation of the bank's assets, and tracing of funds to the receiver. The sole excep-

(3)

tions are in favor of the United States incident to the bank's circulating notes and certain certified checks given it in payment of taxes or duties. *Cook County National Bank* v. *United States, supra; Davis* v. *Elmira Savings Bank, supra; Blakey* v. *Brinson*, 286 U. S. 254; *Larabee Flour Mills* v. *First National Bank*, 13 Fed. (2nd) 330, certiorari denied 273 U. S. 727. On the question of tracing of funds all doubts are to be resolved in favor of the receiver who is the trustee for general creditors. *Schuyler* v. *Littlefield*, 232 U. S. 707; *St. Louis & San Francisco Railroad* v. *Spiller*, 274 U. S. 304; *Cunningham, Trustee of Ponzi* v. *Brown*, 265 U. S. 1. As stated in Note 19 to the opinion of the Supreme Court of the United States in *Texas & Pacific Railroad Company* v. *Pottorff, Receiver of the First National Bank of El Paso*, decided February 5, 1934 "the claimant has the burden of identifying the property in its original or altered form. *Schuyler* v. *Littlefield*, 232 U. S. 707. It is not enough to show that at the time of receipt the general assets of the insolvent were increased or that debts were discharged."

Cases decided by the Supreme Court of the United States during this term to date clearly reflect the intent of the court of last resort to follow its long line of decisions protecting the rights of the depositors of insolvent national banks. Four cases affecting these banks have been decided at this

term to date. Two decisions affirm the Appellate Court decisions favorable to depositors (*City of Marion* v. *Sneeden*, decided February 5, 1934 and *Texas & Pacific Railroad* v. *Pottorff*, decided February 5, 1934) and two Appellate Court decisions adverse to depositors were reversed (*Dakin* v. *Bayly*, 290 U. S. 143 and *Bosworth* v. *Continental Illinois Bank*

(4)

& Trust Company, decided February 8, 1934). The recent decisions of the United States Circuit Court of Appeals, Seventh Circuit, except in the present case, are in complete accord with the trend of decisions of the Supreme Court of the United States and other circuits. *Allied Mills Inc.* v. *Horton*, 65 Fed. (2nd) 708; *Connolly* v. *Alice M. Lang*, 68 Fed. (2nd) 199. The tracing of funds principle applied by this court in the instant case is directly involved in other cases that have been decided by United States District Courts of this circuit, which cases will later be presented to this court for review. Most claims against insolvent national banks are presented to the Comptroller of the Currency incident to the *quasi* judicial function he exercises under the provisions of Section 194, Title 12, U. S. C. A. Accordingly the tracing of funds principle applied in the instant case has a distinct class aspect.

The Question Involved in the Petition for Rehearing.

(B) The sole contention presented by the receiver on rehearing is that on the record in this case the claims based upon the following four items are general only, except possibly to the extent of $643.23, because of the absolute inability of the plaintiff to affirmatively trace proceeds in excess of this amount into the hands of the receiver:

Charles Graff mortgage note and interest	$3,183.78
W. C. Sommer mortgage note and interest	1,058.98
Ten shares, Farmers Bank stock and dividend	3,030.00
Veesaert notes and interest	1,597.31

(5)

As to the Graff item, the record (p. 51) evidences "that on April 12, 1929, said Charles Graff deposited with the Farmers National Bank of Pekin, Illinois, the sum of $14,013.64 * * *". The relationship created by this general deposit was that of debtor and creditor and not that of trustee and *cestui que trust*, hence it is unnecessary to discuss the ultimate disposi-

tion of the items that went to make up this deposit. So far as the record evidences the most that can be said is that the deposit was general but for a special purpose, creating the relationship of debtor and creditor. *Blakey* v. *Brinson, supra; Keyes* v. *Paducah & Illinois Railroad,* 61 Fed. (2nd) 611. The record (p. 54) evidences that "on April 12, 1929, the said defendant bank acting by and through T. W. Mott, its cashier, issued to Frank F. Reis, who was then vice president of said defendant bank, two certain certificates of deposit, one No. 116,062 in the principal sum of $3,000, and the other, No. 116,063, in the sum of $183.78;" Apparently these certificates of deposit were paid for by charges against Graff's pre-existing general credit balance. At any rate the claimant has not proved the contrary. It thus appears that the receiver is required to account for only what the bank received, a mere transfer of bookkeeping credits, hence that the tracing of funds principle of *Schumacher* v. *Harriet,* 52 Fed. (2nd) 817 is inapplicable. *Blakey* v. *Brinson, supra; Allied Mills Inc.* v. *Horton, supra; Connolly* v. *Alice M. Lang, supra; Larabee Flour Mills* v. *First National Bank, supra; Ellerbe* v. *Studebaker Corp.* 21 Fed. (2nd) 933 (opinion by Judge Parker); *City of Miami* v. *First National Bank,* 69 Fed. (2nd) 346.

All that is said concerning the Graff item is also applicable to the Sommer item. The record (p. 55) evidences that Mr.

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Sommer had a pre-existing credit balance in this now insolvent national bank of $192.50 on March 27, 1929. On that date there was credited to Mr. Sommer's account a check in the amount of $14,055.60, also drawn on the now insolvent national bank, increasing the credit balance accordingly. The relationship as to this total credit balance was that of debtor and creditor and not that of trustee and *cestui que trust. Blakey* v. *Brinson, supra; Allied Mills* v. *Horton, supra; Connolly* v. *Lang, supra; Keyes* v. *Paducah & Illinois Railroad, supra; Swan* v. *Childrens Home Society,* 67 Fed. (2nd) 84, certiorari denied January 8, 1934. The record (p. 57) evidences that Sommer's general deposit balance was charged with the sum of $1,058.98 on April 16, 1929. It thus appears that the receiver is required to account for what the bank received only, a mere transfer of a pre-existing credit balance, and that the tracing of funds principal of the Harriet decision

is not involved in this item. Such a claim is general only under the authorities cited in the discussion of the Graff item.

As to the 10 shares of Farmers bank stock and dividend thereon the situation is the same. The record (p. 50) evidences that Cullinan paid for the stock out of a credit balance of $4,000, built up on the books of the bank through a loan made by the bank to Cullinan. This transaction brought no new money into the bank, but amounted to a mere transfer of credits. The relationship between the bank and Cullinan as to the credit balance of $4,000 so built up, was that of debtor and creditor, under the authorities cited in the preceding two paragraphs, hence all the bank received was a transfer of bookkeeping credits for which the receiver stands ready to

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account as a general claim only. The tracing of funds principle of the Harriet decision is not involved. The claimant cannot be concerned with the bank's collection of the note from Cullinan or whether or not the note was collected. This was a separate contract transaction between Cullinan and the bank as to which the claimant is a stranger. *Allied Mills* v. *Horton, supra; Larabee Flour Mills* v. *First National Bank of Dublin,* 69 Fed. (2nd) 351. The dividend of $30 was likewise a mere transfer of credit which did not create a *res* that could be the subject of a trust, hence can be made the basis for a general claim only. *Blakey* v. *Brinson, supra.*

The Veesaert notes and interest item is the only one presenting the question of tracing of funds that could possibly involve the Harriet principle. The record (p. 58) evidences that the now insolvent national bank received as the proceeds of these five mortgage bonds a check in the amount of $1,597.31, drawn on the Edwardsville National Bank & Trust Company, an outside bank. The proceeds of this check are specifically traceable (Rec., 58) as of December 13, 1930, into the closed national bank's account with the First National Bank of Chicago, hence are incapable of being traced into any other account or fund of the now insolvent national bank. The record (p. 59) evidences that the low balance in that account thereafter was in the sum of $643.24 on October 27, 1931. The record (pp. 59 and 60) evidences that the closed bank's balance at suspension of $10,827.03, containing this low balance of $643.24, *the maximum amount that can be claimed to be the property of this claimant under the settled federal rule,* was applied in reduction of its indebtedness to the First National Bank of Chicago but that collateral of

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value was later returned to the receiver upon an advance of funds totaling approximately $53,000, belonging to the general creditors. The receiver readily concedes that the claimant has an equitable lien upon this returned collateral to the extent of $643.24 only, subject to a possible pro rating with others similarly situated and payable only after the receiver has covered the advance of general creditors' funds. For the proposition that under these circumstances the trust fund was dissipated except to the extent of the low balance of $643.24 the receiver cites *Titlow* v. *McCormick*, 236 Fed. 209; *American Can Company* v. *Williams*, 176 Fed. 816, Aff. 178 Fed. 420; *Nyssa-Arcadia Drainage Dist.* v. *First National Bank*, 3 Fed. (2nd) 648; *Marvin* v. *Martin*, 20 Fed. (2nd) 746 and *People ex rel Nelson* v. *Peoples State Bank*, 354 Ill. 519, decided by the Illinois Supreme Court December 22, 1933. The single federal authority to the contrary, *Schumacher* v. *Harriet*, 52 Fed. (2nd) 817, will be discussed separately.

Although the Supreme Court of the United States decided the case of *Blakey* v. *Brinson* on the relationship question and did not find it necessary to discuss augmentation and tracing, these questions were fully briefed by the receiver. The following excerpt from the receiver's brief in that case is pertinent to the Veesaert item:

> "Decisions in the federal courts involving the mingling of trust funds with balances in correspondent banks, insisting upon specific following and negativing any idea of a general lien.
>
> Second Circuit:
>
> *American Can Co.* v. *Williams*, 176 Fed. 816 (C. C. N. Y., 1908), affirmed in 178 Fed. 420 (C. C. A. 2, 1910).

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> Fourth Circuit:
>
> *Marshburn* v. *Williams*, 15 Fed. (2) 589 (D. C., N. C., 1926).
>
> *Ellerbe* v. *Studebaker Corp. of America*, 21 Fed. (2nd) 933 (C. C. A. 4, 1927).
>
> Fifth Circuit:
>
> *Clark Sparks & Sons Mule & Horse Co.* v. *Americus Nat. Bk.* 230 Fed. 738 (D. C., Ga., 1916).
>
> *Washington Loan & Banking Co.* v. *Fourth Nat. Bank of Macon*, 38 F. (2) 772 (C. C. A. 5, 1930).
>
> *Sanders* v. *Stevens*, 51 F. (2) 743 (D. C., Miss., 1931).

Sixth Circuit:

Board of Commissioners of Crawford County v. *Patterson*, 149 Fed. 229 (C. C., Ohio, 196), affirmed in *Same* v. *Strawn*, 157 Fed. 49 (C. C. A. 6, 1907).
Brennan v. *Tillinghast*, 201 Fed. 609 (C. C. A. 6, 1913).

Eighth Circuit:

Lucas County v. *Jamison*, 170 Fed. 338 (C. C. Ia., 1908).
Macy v. *Roedenbeck*, 227 Fed. 346 (C. C. A. 8, 1915).
State Bank of Winfield v. *Alva Security Bank*, 232 Fed. 847 (C. C. A. 8, 1916).
Dudley v. *Richards*, 18 F. (2nd) 876 (C. C. A. 8, 1927).
Bartholf v. *Millett*, 22 F. (2nd) 538 (C. C. A. 8, 1927).
Gwynn v. *Spurway*, 28 F. (2nd) 37 (D. C., Ia., 1928).
Cuttell v. *Fluent*, 51 F. (2nd) 974 (C. C. A. 8, 1931).

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Ninth Circuit:

Titlow v. *McCormick*, 236 Fed. 209 (C. C. A. 9, 1916).
United States Nat. Bank of Centralia v. *City of Centralia*, 240 Fed. 93 (C. C. A. 9, 1917), cert. den. sub. nom. *City of Centralia* v. *Titlow*, 243 U. S. 656 (1917).
First Nat. Bank of Forsyth v. *Fidelity & Deposit Co.* 48 F. (2nd) 585 (C. C. A. 9, 1931).

Tenth Circuit:

Anadarko Cotton Oil Co. v. *Litteer*, 300 Fed. 222 (D. C., Okla., 1924).
Dickson v. *First Nat. Bank of Buffalo, Okla.* 26 F. (2nd) 411 (C. C. A. 8, 1928)."

The receiver respectfully submits that a final decision of this court allowing the plaintiff a preferred claim in excess of the amount of $643.24 would be in conflict with the decisions cited immediately above; with the decisions of the Supreme Court of the United States (*Schuyler* v. *Littlefield*, 232 U. S. 707; *Cunningham, Trustee of Ponzi* v. *Brown*, 265 U. S. 1 and *St. Louis & San Francisco Railroad* v. *Spiller*, 274 U. S. 304); and with the decisions of this court in *Allied Mills* v. *Horton, supra* and *Connolly* v. *Lang, supra.*

The Soundness or Unsoundness of the Tracing of Funds Principle of *Schumacher* v. *Harriet*, 52 Fed. (2nd) 817.

(D) The opinion of this court on April 17, 1934 in the instant case as to the tracing of funds feature relies almost exclusively on *Schumacher* v. *Harriet*, 52 Fed. (2nd) 817. The

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receiver respectfully submits that the tracing of funds principle of the Harriet case receives no support from the following cases cited by this court on page 4 of the opinion, which are the cases cited by the appellee on page 9 of his brief:

Central National Bank v. *Insurance Co.* 104 U. S. 54.
Poisson v. *Williams*, 15 Fed. (2nd) 582.
Brennan v. *Tillinghast*, 201 Fed. 609.
Empire State Surety Co. v. *Carroll County*, 194 Fed. 593.

On the contrary the receiver asserts that all of the above cases except *Schumacher* v. *Harriet* support the contentions set out in this petition for rehearing.

It will be noted that the case of *Schumacher* v. *Harriet*, 52 Fed. (2nd) 817 was a companion case to that of *Schumacher* v. *Brinson*, 52 Fed. (2nd) 821. Certiorari was applied for in the Brinson case only and the Appellate Court's opinion unanimously reversed in 286 U. S. 254. It is the opinion of the Comptroller of the Currency that the decision of the Supreme Court of the United States in the Brinson case reversed the Harriet decision in principle. The Harriet decision is classified as "indirectly overruled by *Blakey* v. *Brinson*" in *Keyes* v. *Paducah & Illinois Railroad Co*, *supra* on page 614. The tracing of funds principle of the Harriet case is characterized as a "novel view" by the United States Circuit Court of Appeals, Fifth Circuit in *Pottorff* v. *Key*, 67 Fed. (2nd) 833. The similar "novel view" of the Appellate Court in the Brinson case was unanimously rejected by the Supreme Court of the United States. The Harriet decision is criticized in 80 Pennsylvania Law Review 587.

A few years ago there was an apparent tendency of the

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United States Circuit Courts of Appeal of the Fourth and Fifth Circuits to liberalize the allowance of preferred claims against insolvent national banks. The liberal rule as to such claims applied in some states, including Florida, with the result that dividends to general creditors are substantially re-

duced, was sought to be imported into the federal decisions, which undoubtedly theretofore followed the strict rule of resolving all doubts in favor of the general depositors. This tendency is evidenced in the opinions in *Ellerbe* v. *Studebaker Corp.* 21 Fed. (2nd) 993 (as to deposits made at the time the collection was made); *Schumacher* v. *Brinson,* 52 Fed. (2nd) 821; *Schumacher* v. *Harriet,* 52 Fed. (2nd) 817; *Davis* v. *McNair,* 48 Fed. (2nd) 494; *City of Miami* v. *First National Bank,* 58 Fed. (2nd) 561.

After the unanimous reversal of the Brinson case by the Supreme Court of the United States the City of Miami case was twice certified to the Supreme Court of the United States and the certificates dismissed on jurisdictional grounds. The recent opinion of the United States Circuit Court of Appeals, Fifth Circuit in that case, reported in 69 Fed. (2nd) 346, allowing a general claim only, contains a clear statement of the present position of that court. The preferred claim originally allowed in *Davis* v. *McNair, supra,* was recently substantially reduced by the Appellate Court in its opinion, reported in 68 Fed. (2nd) 935, and a petition for certiorari is now pending in the Supreme Court of the United States, supplemented with a brief *amicus curiae* on behalf of the Comptroller of the Currency. In its recent decision in *Allied Mills* v. *Horton* this court declined to follow the substance rather than form principle of *Ellerbe* v. *Studebaker Corp.,* which is the only

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feature objected to by the receivers of insolvent national banks. Also the United States Circuit Court of Appeals, Fifth Circuit declined to follow that principle in its recent affirmance of the trial court in *Larabee Flour Mills* v. *First National Bank of Dublin,* 69 Fed. (2nd) 351. This last case was also certified to the Supreme Court of the United States on two occasions and the certificates dismissed on jurisdictional grounds.

It thus appears that the Harriet decision stands alone for the tracing of funds principle announced therein. The principle has never been affirmed either by the United States Circuit Court of Appeals of the Fourth, or any other circuit. The opinion has been criticized by the authorities cited above and the receiver submits it should not be followed in the instant case. The receiver believes the following excerpt from the opinion of the United States Circuit Court of Appeals, Fifth Circuit in *City of Miami* v. *First National Bank, supra,* page 349, particularly applicable to the instant case as this opinion was written after careful consideration by the court

of the cases referred to as tending to liberalize the federal preferred claim rule:

> "We have, we think, already in other cases, *McNair* v. *Oesterreicher*, 63 F. (2nd) 876; *Spurway* v. *Frick Co.* 63 Fed. (2nd) 875; *Smith* v. *Zemurray*, 69 Fed. (2nd) 5; *Pottorff* v. *Key*, 67 F. (2nd) 833; *Wisdom* v. *Keen*, 69 Fed. (2nd) 349, made it sufficiently plain that to obtain preferential treatment in the distribution of the assets of failed banks, one seeking to charge the fund in the hands of the receiver for the benefit of all the creditors, as being his property of its proceeds, has a heavy burden of proof, and unless he clearly and certainly identifies the fund he must fail. *Schuyler* v. *Littlfield*, 232 U. S.
>
> (14)
>
> 707, 34 S. Ct. 466, 58 L. Ed. 806. We do not understand anything decided in the *Miami Bank Case, supra*, contravenes these views. Any expression in it, which admits of a contrary construction, is expressly disapproved."

For the above reasons it is respectfully submitted that a rehearing of this case should be granted; that the entire claims based upon the Graff, Sommer, and bank stock items should be classified as general only, and that the claim based on the Veesaert item should be classified as general only except as to the sum of $643.24, the total amount traceable to the receiver, payable only after the receiver has been reimbursed from the collateral, for the general creditors' funds advanced. Such a disposition affirms the finding that the bank received these bankruptcy assets as trustee which requires the receiver to account for the full proceeds thereof traceable into his hands. Such proceeds consist exclusively of the sum of $643.24, the balance received on the Veesaert item having been dissipated by the bank prior to its suspension. All proceeds received on all of the other items consisted of mere transfers of bookkeeping credits resulting in general claims only.

Your petitioner further prays that upon hearing of this petition for rehearing and answer thereto he may be permitted by this court to argue orally upon the merits of said petition for rehearing.

Respectfully submitted,

JESSE BLACK, JR.,
Attorney for Petitioner.

JOHN F. ANDERSON,
Of Counsel for Petitioner.

Endorsed: Filed May 17, 1934. Frederick G. Campbell, Clerk.

And afterwards, to-wit: On the twenty-fourth day of May, 1934, there was filed in the office of the Clerk of this court an answer to the petition for rehearing, which said answer to the petition for rehearing is in the words and figures following, to-wit:

No. 5076

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

October Term, A. D. 1933.

Ross C. Adams, Receiver of the Farmers National Bank, of Pekin, Illinois,
Appellant-Petitioner,
vs.
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt,
Appellee-Respondent.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

Honorable
Louis FitzHenry,
Trial Judge.

ANSWER OF APPELLEE TO PETITION FOR REHEARING.

Counsel for Appellant:

JESSE BLACK, JR.,
Farmers National Bank Building, Pekin, Illinois.
JOHN F. ANDERSON,
Care Comptroller of the Currency,
Washington, D. C.

Counsel for Appellee:

IRA J. COVEY,
Jefferson Building,
Peoria, Illinois.
EDWIN L. COVEY,
Jefferson Building,
Peoria, Illinois.

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Summary of Argument.

There is no assignment of error in any way questioning the correctness of the findings of fact of the District Court. In legal effect these facts are admitted. The trust funds were in possession of the bank when it closed, and passed to the receiver, and are now held by him. This entitled appellee to a priority..... *2

The Supreme Court in the case of Blakey v. Brinson, 286 U. S. 254, did not reverse the case of Schumacher v. Harriett, 52 Fed. (2nd) 817, in principle, for the reason that the Court in the Brinson case did not pass on the question of tracing of funds, but based its decision on the fact that no trust relation existed..... 3

The same is true with regard to the holding in the case of Keyes v. Paducah & Illinois Railroad Co., 62 Fed. (2nd) 611 3

The only case which can be found which may be said to be at variance with the Harriett case is American Can Co. v. Williams, 176 Fed. Rep. 816, decided by the Western District of New York..... 3

List of Cases.

American Can Co. v. Williams, 176 Fed. Rep. 816..... 4

Blakey v. Brinson, 286 U. S. 254, 76 L. Ed. 1089..... 2

Connolly v. Lang, 68 Fed. (2nd) 199, 201..... 2

Keyes v. Paducah & Illinois Railroad Co., 61 Fed. (2nd) 611 3

Schumacher v. Harriett, 52 Fed. (2nd) 817..... 2

* Small figures in parentheses show commencement of original page.

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

October Term, A. D. 1933.

No. 5076.

Ross C. Adams, Receiver of the Farmers National Bank, of Pekin, Illinois,
Appellant-Petitioner,
vs.
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt,
Appellee-Respondent.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

Honorable
Louis FitzHenry,
Trial Judge.

ANSWER OF APPELLEE TO PETITION FOR REHEARING.

The petition for rehearing admits the existence of a trust relationship and the augmentation of the bank's assets, but insists that the trust funds were not sufficiently traced into the hands of the Receiver (See pps. 2 and 14 of Petition).

On pages 2 and 3 of its Opinion this Court said:

> "Upon submission the Court made findings of fact and rendered its conclusions of law favorable to appellee with respect to the four items in controversy. The

> Court's findings which are material to the question here presented are substantially as follows: That the Bank received the four items of collateral as an unlawful and recoverable preference and treated them as cash and shortly thereafter converted them into cash which was intermingled with the cash of the Bank and treated by it as its own; that when the Bank closed it had on hand in cash and cash items $36,054.76, which afterwards went into the hands of the Receiver; that the least amount in

cash and cash items in the Bank during the period from February 5, 1929, to the close of business on January 7, 1932, was $30,548.61; that the Bank by collecting bankrupt's notes and bonds and by sale of his bank stock without the knowledge or consent of the trustee, held the proceeds of such collections and sale amounting to $8,870.07, as a trustee *ex maleficio;* and that said funds were in the possession of the Bank when it closed."

On pages 12 to 16 of our original brief, we pointed out that there is no assignment of error in any way questioning the correctness of these findings. In legal effect these facts are admitted, and being admitted the ruling of the Trial Court was right beyond question. The trust funds were in the possession of the Bank when it closed and passed to the Receiver, and are now held by him. This entitles appellee to a priority. See *Connolly* v. *Lang,* 68 Fed. (2) 199, 201, Point 1, (C. C. A. 7).

* * *

On page 11 of the petition, counsel for Receiver say:

"It is the opinion of the Comptroller of the Currency that the decision of the Supreme Court of the United States in the Brinson case (*Blakey* v. *Brinson,* 286 U. S. 254, 76 L. Ed. 1089) reversed the Harriett (*Schumacher* v. *Harriett,* 52 Fed. (2) 817 decision in principle."

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But, on page 8, they admit that the Supreme Court in the *Brinson* case "did not find it necessary to discuss augmentation and tracing." Aside from this admission, it will be noted that the Court, on page 260, stated that two questions were raised: *First,* That no trust ever came into existence; and, *Second,* That the check did not augment the Bank's funds and that the proceeds could not be traced into the hands of the Receiver. The Court, thereupon, said:

"As we conclude that the petitioners' first contention is well taken, it is unnecessary to consider the second."

On page 11 of their petition, counsel for the appellant say that the Harriett decision is classified as "indirectly overruled by *Blakey* v. *Brinson* in *Keyes* v. *Paducah & Illinois Railroad Co.,*" 61 Fed. (2) 611, (C. C. A. 6). But, the Court, on page 612, said:

"The doctrines of augmentation and tracing are, however, to be considered only if the trust relationship exists, otherwise they are unimportant."

On pages 613 and 614, at Point 10, the Court found that no trust fund existed, and, therefore, did not consider augmentation and tracing, and not having considered the question of tracing, could not have intended to say that the *Harriett* case had been indirectly overruled by *Blakey* v. *Brinson* with reference to tracing.

* * *

Counsel for the Receiver cite a long list of cases on pages 8, 9 and 10 of their petition, which are copied from the brief in the Supreme Court in the *Blakey* case which they say are in conflict with the holding in the *Harriett* case, but we are of the opinion that the only case which can be found which may be said to be at variance with the *Harriett* case is that of *American Can Co.* v. *Williams*, 176 Fed. Rep. 816, decided by

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the Western District of New York.

* * *

The country at the present time is undergoing many important changes, and it is many times difficult to keep up with them. It may well be that these changes are materially affecting the administration of the law. Judge Parker, in the *Harriett* case, on page 819, Point 8, shows how the doctrine of tracing funds has been greatly liberalized in recent years.

It seems to us that the rule laid down by Judge Parker with reference to tracing funds is equitable, and much more so than the one contended for by counsel for the appellant.

But whether or not the decision of the *Harriett* case is to be adopted as stating the correct rule of law, we insist that under the findings of the Trial Court,—the correctness of which has not been legally challenged,—the judgment of this Court affirming the District Court is well founded.

Respectfully submitted,

IRA J. COVEY,
EDWIN L. COVEY,
Attorneys for Appellee.

Endorsed: Filed May 24, 1934, Frederick G. Campbell, Clerk.

And afterwards, to-wit: On the seventh day of June, 1934, there was filed in the office of the Clerk of this court an appearance for the appellant, which said appearance is in the words and figures following, to-wit:

UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

October Term, A. D. 1933, April Session, 1934.

Ross C. Adams, Receiver, etc.
5076 *vs.*
Edwin V. Champion, Trustee, etc.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

I hereby enter my own appearance and the appearance of John F. Anderson, of Washington, D. C., as attorneys for Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, Appellant-Petitioner in the above entitled cause.

JESSE BLACK, JR.
JOHN F. ANDERSON.

Endorsed: Filed June 7, 1934, Frederick G. Campbell, Clerk.

And afterwards, to-wit: On the thirteenth day of June, 1934, the following further proceedings were had and entered of record, to-wit:

Wednesday, June 13, 1934.

Court met pursuant to adjournment and was opened by proclamation.

Before:

Hon. Samuel Alschuler, Circuit Judge.
Hon. Evan A. Evans, Circuit Judge.
Hon. William M. Sparks, Circuit Judge.

Ross C. Adams, Receiver, etc.
5076 *vs.*
Edwin V. Champion, Trustee.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

It is ordered by the court that the petition for a rehearing in this cause be, and the same is hereby denied.

And afterwards, to-wit: On the fourteenth day of June, 1934, the mandate of this court issued to the District Court of the United States for the Southern District of Illinois, Northern Division.

And afterwards, to-wit: On the fifteenth day of June, 1934, there was filed in the office of the Clerk of this court a motion for stay of mandate, together with affidavits and proof of service, which said motion, affidavits and proof of service are in the words and figures following, to-wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5076.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,
Appellant-Petitioner,
vs.
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, a Bankrupt,
Appellee-Respondent.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

Hon. Louis FitzHenry, Trial Judge.

Your petitioner, Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, respectfully shows to this Court that he was advised on this day by his attorney, Jesse Black, Jr., that petition for re-hearing in the above entitled cause had been overruled.

Your petitioner further shows to this Court that in this cause, by instructions of the Comptroller of the Currency of the United States, he intends filing and will file a petition for certiorari to the Supreme Court of the United States.

Your petitioner therefore moves the Court for a stay of mandate in the above entitled cause.

Dated this 14th day of June, A. D. 1934.

ROSS C. ADAMS,
Receiver of the Farmers National Bank of Pekin, Illinois.

JOHN F. ANDERSON,
JESSE BLACK, JR.,
Attorneys for Ross C. Adams, Receiver of Farmers Nat'l Bank, Pekin, Ill.

State of Illinois,
County of Tazewell. ss.

ROSS C. ADAMS, Receiver of the Farmers National Bank of Pekin, Illinois, being first duly sworn upon his oath, deposes and says that he has read the foregoing motion and petition by him subscribed and the same is true in substance and in fact.

Further deponent saith not.

Ross C. Adams.

Subscribed and sworn to before me this 14th day of June, A. D. 1934.

(Seal)

Hester E. Holland,
Notary Public.

In the United States Circuit Court of Appeals

For the Seventh Circuit.

No. 5076.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,
Appellant-Petitioner,
vs.
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, a Bankrupt,
Appellee-Respondent.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.
Hon.
Louis FitzHenry,
Trial Judge.

AFFIDAVIT.

JESSE BLACK, JR., being first duly sworn upon his oath, deposes and says that he is attorney for Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, Appellant-Petitioner in the above entitled cause; that he did on Thursday, June 14, 1934, at 2:30 o'clock P. M. deliver personally to Ira J. Covey and Edwin L. Covey, attorneys for Edwin

V. Chamption, Trustee in Bankruptcy of John Fitzgerald, a bankrupt, Appellee-Respondent in the above entitled cause, a true and correct copy of the said motion and petition for stay of mandate, and that he attaches to this affidavit the receipt of the said Ira J. Covey and Edwin L. Covey for said copy of motion.

Further deponent saith not.

JESSE BLACK, JR.

Subscribed and sworn to before me this 14th day of June, A. D. 1934.

HESTER E. HOLLAND,
Notary Public.

(Seal)

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5076.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,
Appellant-Petitioner,
vs.
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, a Bankrupt,
Appellee-Respondent.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.
Hon.
Louis FitzHenry,
Trial Judge.

Received from Jesse Black, Jr., attorney for Appellant-Petitioner in the above entitled cause, a true and correct copy of the motion and petition for stay of mandate.

Dated this 14th day of June, A. D. 1934 at 2:30 o'clock P. M.

IRA J. COVEY,
EDWIN L. COVEY,
Attorneys for Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, a Bankrupt.

Endorsed: Filed Jun 15, 1934. Frederick G. Campbell, Clerk.

And on the same day, to-wit: On the fifteenth day of June, 1934, the following further proceedings were had and entered of record, to-wit:

Friday June 15, 1934.

Court met pursuant to adjournment and was opened by proclamation.

Before:

Hon. Samuel Alschuler, Circuit Judge.

Ross C. Adams, Receiver, etc.
5076 *vs.*
Edwin V. Champion, Trustee, etc.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.

Now this day comes counsel for appellant and presents a motion for recalling and staying the mandate of this court, pending a petition to the Supreme Court of the United States for a writ of certiorari.

On consideration whereof: It is now here ordered that the mandate in this cause be, and the same is hereby recalled and stayed until the further order of this court.

It is further ordered that counsel for appellant proceed with diligence and promptly file the petition for a writ of certiorari in the Supreme Court of the United States and, upon the filing of said petition file in this court proof of the filing of said petition in said court.

And afterwards, to-wit: On the 23rd day of June, 1934, there was filed in the office of the Clerk of this court a withdrawal of appearance of counsel for appellant, which said withdrawal of appearance of counsel for appellant is in the words and figures following, to-wit:

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

No. 5076.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois,
Appellant-Petitioner,
vs.
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, a Bankrupt,
Appellee-Respondent.

Appeal from the District Court of the United States for the Southern District of Illinois, Northern Division.
Hon.
Louis FitzHenry,
Trial Judge.

We, the undersigned, hereby withdraw our appearance as attorneys for Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, Appellant in the above entitled cause.

Dated this 14th. day of June, A. D. 1934.

FRANKLIN L. VELDE.
WM. S. PRETTYMAN.

Endorsed: Filed June 23, 1934. Frederick G. Campbell, Clerk.

UNITED STATES CIRCUIT COURT OF APPEALS

For the Seventh Circuit.

I, Frederick G. Campbell, Clerk of the United States Circuit Court of Appeals for the Seventh Circuit, do hereby certify that the foregoing printed pages, numbered from 79 to 118, inclusive, contain a true copy of the proceeding had and papers filed (excepting the briefs of counsel, petition for rehearing and answer thereto) in the case of

Ross C. Adams, Receiver of The Farmers National Bank of Pekin, Illinois,

Appellant,

vs.

Edwin V. Champion, Trustee in Bankruptcy, etc.,

Appellee,

No. 5076, October Term, 1933, as the same remains upon the files and records of the United States Circuit Court of Appeals for the Seventh Circuit.

In Testimony Whereof I hereunto subscribe my name and affix the seal of said United States Circuit Court of Appeals for the Seventh Circuit, at the City of Chicago, this 28th day of June, A. D. 1934.

(Seal)

FREDERICK G. CAMPBELL,
Clerk of the United States Circuit Court of Appeals for the Seventh Circuit.

[fol. 120] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed October 22, 1934.

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Seventh Circuit is granted, and the case is assigned for argument immediately following Nos. 338 and 340.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 39,002. U. S. Circuit Court of Appeals, Seventh Circuit. Term No. 374. Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, petitioner, vs. Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt. Petition for writ of certiorari and exhibit thereto. Filed September 12, 1934. File No. 374, O. T., 1934.

FILE COPY

SEP 12 1

CHARLES ELMORE

Supreme Court of the United States

OCTOBER TERM, 1934.

No. 374

ROSS C. ADAMS, Receiver of the Farmers National Bank of Pekin, Illinois, Petitioner,

vs.

EDWIN V. CHAMPION, Trustee in Bankruptcy of JOHN FITZGERALD, Bankrupt, Respondent.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit and Brief in Support Thereof.

JESSE BLACK, JR.,
JOHN F. ANDERSON,
Attorneys for Petitioner.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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Supreme Court of the United States

OCTOBER TERM, 1934.

No. ———.

ROSS C. ADAMS, Receiver of the Farmers National Bank of Pekin, Illinois, Petitioner,

vs.

EDWIN V. CHAMPION, Trustee in Bankruptcy of JOHN FITZGERALD, Bankrupt, Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

To the Honorable the Supreme Court of the United States:

Your petitioner, Ross C. Adams as Receiver of the Farmers National Bank of Pekin, Illinois, respectfully prays that a writ of certiorari issue to review the judgment and decree of the United States Circuit Court of Appeals for the Seventh Circuit, rendered in the above case (R. 82).

I.

THE CASE.

The United States District Court for the Southern District of Illinois, Northern Division, rendered judgment and decree (R. 69) allowing Edwin V. Champion, Trustee in Bankruptcy for John Fitzgerald, bankrupt, petitioner, a

priority claim against the cash in the Farmers National Bank of Pekin, Illinois, at its suspension. The Receiver of the suspended Bank appealed to the Circuit Court of Appeals and the judgment of the District Court was affirmed (R. 82) and Petitioner now seeks a review of the Decree of the Circuit Court of Appeals, Seventh Circuit. Petition for rehearing was denied June 13, 1931 (R. 113).

II.

SUMMARY OF MATTERS INVOLVED.

On June 24, 1930, the District Court of the United States, Southern District of Illinois, Northern Division, decreed (R. 24) that the Farmers National Bank of Pekin, Illinois, had obtained an unlawful preference from John Fitzgerald, a bankrupt, by taking certain collateral for his indebtedness, and directed the bank to turn over to Edwin V. Champion, the bankruptcy trustee (respondent in this case) said collateral or the proceeds. Prior to the entry of this decree and on January 7, 1932, the Farmers National Bank of Pekin, Illinois, had become insolvent and Ross C. Adams (the petitioner in this case), was appointed Receiver by the Comptroller of the Currency to wind up its affairs. The bank Receiver, pursuant to the aforesaid decree of the District Court, surrendered to the bankruptcy trustee all collateral received from the bankrupt (R. 37), except four items of an aggregate value of $8870.07 which had passed out of the hands of the bank prior to its suspension. The bank Receiver contended that the claim of the bankruptcy trustee in the amount of $8870.07 was general and not preferred, because the proceeds of the four items were not traceable into his hands as Receiver, whereupon the trustee in bankruptcy filed a petition in said District Court (R. 31) (this case) praying that the bank Receiver be directed to pay this sum in full. The bank Receiver answered averring that there had been no augmentation of the funds of the bank incident to the four items and that the proceeds

could not be traced into his hands as Receiver. After a hearing on the petition (R. 31-38), answer (R. 40), amendment (R. 44), and stipulation of facts (R. 49), the trial court held (R. 66-69), that the bank received the four items as trustee; that they were converted into cash by the bank, and used as its own, and by decree entered July 7, 1933 (R. 69), allowed the bankruptcy trustee a priority claim of $8870.07 against the bank Receiver.

The bank Receiver appealed to the United States Circuit Court of Appeals, Seventh Circuit (R. 71), and the Appellate Court affirmed the judgment of the District Court. Opinion, reported 70 Fed. (2d) 956, and set out in the record, page 82. Rehearing was denied June 13, 1934 (R. 113).

The record facts concerning the issue (which is the tracing of proceeds to the bank Receiver as to the four items received by the bank from the bankrupt and disposed of by it prior to suspension), are as follows:

ITEM 1. This item consisted of 10 shares of the capital stock of the Farmers National Bank, sold by it on February 9, 1929, to R. A. Cullinan for the sum of $3000, payment being effected by a charge against Mr. Cullinan's credit balance in the Farmers National Bank (R. 50, 51). A portion of the preferred claim allowed as to this item consisted of a $30 dividend on this stock (R. 50).

If it be material (which the bank Receiver denies) the credit balance from which payment for the above stock by Cullinan was effected was built up on the same day from the proceeds of a loan in the amount of $4000 made by the bank to Mr. Cullinan (R. 50).

ITEM 2. This item consisted of the Charles Graff note in the total amount of $3483.78, paid by Graff on April 12, 1929, by a charge against his deposit balance in the Farmers National Bank whereby two certificates of deposit were issued by the bank to its Vice President Reise and charged against Graff's account, in exchange for which the note was delivered to Graff (R. 51 and 54).

If it be material (which the bank Receiver denies) Mr. Graff deposited to his credit in the Farmers National Bank on April 12, 1929, items totaling $14,013.64. The proceeds of these items are traceable into the accounts of the Farmers National Bank with correspondent banks as follows: (1) Into the First National Bank of Peoria, Illinois, the low balance thereafter in said account being $51.41 (R. 51); (2) Into the First National Bank of Chicago, the low balance thereafter in said account being $70.54 (R. 52); and (3) Into a bank subsequently merged with the Commercial Merchants National Bank & Trust Company of Peoria, the low balance thereafter in said account being $351.94 (R. 53). The record does not contain affirmative proof that the bank receiver ultimately received anything from the correspondent banks having these low balances, except as to the First National Bank of Chicago where the sum of $643.24 admittedly due on the fourth item contains the prior low balance of $70.54, consequently even though these facts were material the claim is general only under the tracing of funds rule applied by this court in *Schuyler v. Littlefield*, 232 U. S. 707, 713.

ITEM 3. This item consisted of the W. C. Sommer note in the total amount of $1058.98 paid by Sommer on April 16, 1929, by a charge against his deposit balance in the Farmers National Bank whereby two certificates of deposit were issued by the bank to its Vice President, Reise, and charged against Sommer's account, in exchange for which the note was delivered to Sommers (R. 54).

If it be material (which the bank Receiver denies) Mr. Sommer deposited to his credit in the Farmers National Bank on March 27, 1929 (R. 55) a check in the amount of $14,055.60, drawn on that bank by T. M. Smith. The credit balance so drawn against by Mr. Smith was built up (R. 56, 57) by a prior deposit to his credit of items totaling $14,308.10. The only items included in Smith's deposit, concerning which the record contains affirmative proof of alleged augmentation and tracing, are items traceable into

the closed bank's balance with the First National Bank of Peoria, the low balance thereafter (November 28, 1930), (R. 51) being in the amount of $51.41, the same low balance referred to under the Graff item above, and items traceable into the now closed bank's balance with the Merchants & Illinois National Bank of Peoria, which later became the Merchants National Bank & Trust Company, the low balance thereafter (December 21, 1931) (R. 53), $351.94 the same low balance referred to under the Graff item above. The record does not contain affirmative proof that the bank receiver ultimately received anything from the correspondent banks having these low balances, consequently even though these facts were material the claim is general only under the tracing of funds rule applied by this court in *Schuyler v. Littlefield*, 232 U. S. 707, 713.

ITEM 4. This item consisted of five Veesaert mortgage bonds, which were involved in certain foreclosure proceedings, in the course of which the Farmers National Bank surrendered said bonds and received a check in the sum of $1597.31, drawn on the Edwardsville National Bank & Trust Company, the proceeds of which ultimately passed to the credit of the Farmers National Bank in its correspondent, the First National Bank, Chicago (R. 58). The low balance of Farmers National Bank in First National Bank thereafter was $643.24 (R. 59). This balance of $643.24 is traceable into the assets collected by the Receiver of Farmers National Bank from the First National Bank, Chicago (R. 59, 60).

If it be material (which the bank Receiver denies) when the Farmers National Bank closed on January 7, 1932, it had on hand in cash items $36,054.76. The least amount in cash items in the Farmers National Bank between February 5, 1929 and the close of business on January 7, 1932, was $30,548.61 (R. 68).

The District Court held that there had been tracing of the proceeds of the four items in question into the cash in

the hands of the Receiver; that the proceeds collected from said items had been intermingled with the cash of the bank and treated as its own (R. 69), and that a preferred claim should be allowed.

The Circuit Court of Appeals in its opinion (R. 86) adopted the doctrine of *Schumacher v. Harriett*, 52 Fed (2) 817, saying that the facts in the Harriett case were analogous to the instant case, and affirmed the District Court's judgment endorsing thereby the doctrine of tracing set forth in the Harriett case (R. 82).

III.

REASONS FOR GRANTING THE WRIT.

The Facts in the Case are not in Dispute. Petitioner Complains of the Construction of Said Facts as a Matter of Law Wherein it was Held That by Virtue of the Doctrine of Schumacher v. Harriett, Supra, Tracing to the Bank Receiving of the Proceeds of the Four Items has Been Shown in the Instant Case.

Petitioner believes that the writ of certiorari should be granted because:

(a) The decision and decree of the Circuit Court of Appeals involves a Federal question relating to the rights of creditors against National Banks under the National Banking Laws, and the decision of the Circuit Court of Appeals appears to be in conflict with the principles of law established in analogous cases by this Honorable Court. *Pottorff v. Texas & Pacific R. R.*, 291 U. S. 245, 261; *Blakey v. Brinson*, 286 U. S. 254, 262; *Schuyler v. Littlefield*, 232 U. S. 707, 710, 713; *Cunningham, Trustee of Ponzi v. Brown*, 265 U. S. 1, 11; *St. Louis and San Francisco R. R. v. Spiller*, 274 U. S. 304, 310.

(b) The decision of the Circuit Court of Appeals in adopting in the instant case the doctrine of *Schumacher v. Harriett, supra*, as to tracing ignores and is in conflict with

the principles of law established by decisions of the Circuit Courts of Appeal in analogous cases in other Circuits. *American Can. Co. v. Williams*, 176 Fed. 816; *American Can Co. v. Williams* (C. C. A. 2), 178 Fed. 420; *Mechanics & Metals National Bank v. Buchanan* (C. C. A. 8), 12 F. (2) 891; *Empire State Surety Co. v. Carroll County* (C. C. A. 8), 194 F. 593; *Farmers National Bank v. Pribble* (C. C. A. 8), 15 F. (2) 175; *Spurway v. Kellogg* (C. C. A. 5), 63 F. (2) 883; *Dickson v. First National Bank* (C. C. A. 8), 26 F. (2) 411; *Schilling v. Rowe* (C. C. A. 9), 64 F. (2) 188; *Burnes National Bank v. Spurway* (C. C. A. 8), 28 F. (2) 40; *First National Bank v. Williams* (C. C. A. 4), 15 F. (2) 585; *Rorebeck v. Benedict Flour & Feed Co.* (C. C. A. 8), 26 F. (2) 440; *Larabee Flour Mills v. First National Bank* (C. C. A. 8), 13 F. 330, certiorari denied 273 U. S. 727; *Beard v. Independent District of Pella City* (C. C. A. 8), 88 F. 375; *Titlow v. McCormick* (C. C. A. 9), 236 F. 209.

The foregoing cases in the various circuits, and the decisions of this Honorable Court, above cited, establish the principles of law *that a preferred claim can be allowed against the estate of an insolvent only where* (1) the relationship is that of trustee and cestui que trust; (2) the transaction with the claimant resulted in augmentation or increase of the assets of the insolvent by the property of the claimant or the proceeds thereof in the form of actual cash or other tangible assets (as distinguished from the establishment and appropriation or dissipation of a deposit or book credit); (3) that such property or assets of the claimant, or other property identified as being in lieu thereof, can be traced into the hands of the receiver or trustee taking over the assets of the insolvent at the time of suspension or bankruptcy, and (4) that the burden of showing the facts of augmentation and tracing is upon the preferred claimant and that the law will not presume augmentation and tracing.

Assuming such principles of law to be controlling in the

establishment of preferred claims, it would appear that the decision of the Circuit Court of Appeals is clearly contrary to such principles for the reasons that augmentation and tracing did not exist in the instant case, except as to the sum of $643.24, the proceeds of the Veesaert bonds included in the low balance in this amount in the account with the First National Bank of Chicago, and the court was in error in its construction of the principles of law relating to augmentation and tracing.

(c) The Circuit Court of Appeals has decided an important question of general law relating to insolvent estates, in a way probably untenable and in conflict with the weight of authority indicated by the foregoing decisions.

(d) The precise kind of case decided by the Circuit Court of Appeals has not, apparently, heretofore been passed upon by this Court. Since the decision of the Circuit Court of Appeals in this case and the decision in the *Schumacher v. Harriett case, supra*, the indications are that if the principles established by the decision in the Schumacher case and in the instant case are permitted to stand, the basis and scope of claims against insolvent national banks in receivership will be very substantially broadened, and a considerable additional number and amount of claims will have to be allowed, to the detriment of the general creditors. We feel that the importance of the case from this aspect alone merits consideration by this Court.

It is felt further that in the interest of establishing uniformity in the various circuits, this Honorable Court should pass upon the questions of law in issue in the instant case, as was done in the case of *Jenkins, Receiver, v. National Surety Co.*, 277 U. S. 258.

WHEREFORE it is respectfully prayed that the petition for writ of certiorari be granted.

JESSE BLACK, JR.,
JOHN F. ANDERSON,
Attorneys for Petitioner.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1934.

No. ———.

ROSS C. ADAMS, Receiver of the Farmers National Bank of Pekin, Illinois, Petitioner,

vs.

EDWIN V. CHAMPION, Trustee in Bankruptcy of JOHN FITZGERALD, Bankrupt, Respondent.

BRIEF IN SUPPORT OF PETITION.

I.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals is reported in 70 Fed. (2nd) 956 and appears in the record at pages 82 to 87. Findings of fact, conclusions of law, and decree of the United States District Court appear in the record at pages 65 to 70.

II.

JURISDICTION.

The decree of the Circuit Court of Appeals was entered April 17, 1934 (R. 87). A petition for rehearing, duly and seasonably filed by the appellant (R. 98 to 107), was denied

on June 13, 1934 (R. 113). Jurisdiction is conferred upon this court to review this cause by writ of certiorari under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 (U. S. C. Title 28, Section 347).

III.

STATEMENT OF CASE.

A statement of the case is set out in the foregoing petition under the caption, "Summary of Matters Involved," to which reference is here made. Such elaboration of the facts as appears to be pertinent to the discussion will be indicated where appropriate.

IV.

SPECIFICATION OF ERRORS.

(a) The Circuit Court of Appeals held that upon the facts stated the proceeds of the plaintiff's property, held in trust, were traceable into the hands of the Receiver. This was error for the reason that according to the undisputed facts said property, or the entire proceeds thereof, were dissipated prior to the suspension of the bank, except as to the sum of $643.24, the low balance in the account with the First National Bank of Chicago, which the bank Receiver concedes belongs to the claimant, subject to a possible prorating among any other preferred claimants who can trace their proceeds into this low balance.

(b) The Circuit Court of Appeals applied the erroneous rule established in *Schumacher vs. Harriett* (C. C. A. 4th) 52 Fed. (2) 817, and held that irrespective of tracing, a preferred claim in the sum of $8870.07 was proper on the ground that the cash in the bank was impressed with a trust in favor of the bankruptcy trustee. This was error for the reasons that (1) a preferred claim cannot properly be allowed against an insolvent estate unless there is augmentation of assets, and a tracing of these assets or the proceeds

thereof to the Receiver or trustee taking over the estate of the insolvent, and (2) the bank at the time of its suspension had no funds belonging to the plaintiff (except the aforesaid low balance of $643.24 in the First National Bank of Chicago), and (3) the cash in the bank and in any of its correspondent banks (except the $643.24 referred to), was not the cash of the claimant but the property of the bank which came from sources other than the bankruptcy estate, and no part thereof was segregated or intended to be segregated for the use of the claimant.

V.

SUMMARY OF ARGUMENT.

Under the Federal rule settled by decisions of this Honorable Court and by decisions of the Circuit Courts of Appeal, one seeking to establish a preferred claim against the funds in the hands of the Receiver of an insolvent National Bank for the benefit of all the creditors must affirmatively prove that a trust relationship exists, that the assets of the bank were augmented by the transaction and that the trust property or its proceeds is traceable into the hands of the bank Receiver. The burden of proof is upon the claimant and must be resolved in favor of the bank Receiver, who is the trustee for general creditors. In the present case the four items in question are conceded by the Receiver to have been acquired by the now insolvent National bank in trust and all were disposed of by the bank prior to its suspension. In exchange for three of the trust items the bank received nothing but transfers of credits already in the bank, and these transfers of credit did not augment the bank's assets and do not permit tracing to the Receiver. In exchange for the fourth item, the Veesaert bonds, the bank received a check in the amount of $1597.31, drawn on an outside bank, which augmented its assets. However, prior to its suspension, these proceeds were dissipated by use of the same in payment of the bank's in-

debtedness, except as to that portion thereof contained in the aforesaid low balance in the First National Bank of Chicago of $643.24, which amount should be fixed as the amount of the preferred claim rather than the sum of $8870.07 erroneously fixed by the Circuit Court of Appeals. The tracing of funds principle of the Harriett decision, *supra*, relied on by the Circuit Court of Appeals in its allowance of a preferred claim in the amount of $8870.07, has *no* application to three of the trust items totaling $7272.76 and its application to any of the items was erroneous because the principle is in clear conflict with the principles contained in the decisions of this Honorable Court, and the decisions of many United States Circuit Courts of Appeal.

VI.

ARGUMENT.

A. The Necessary Elements of a Preferred Claim, and the Rule Stated as to Augmentation and Tracing.

Section 5236 United States Revised Statutes (Section 194, Title 12, U. S. C. A.), relating to insolvent national banks in receivership, contemplates that the assets thereof shall be distributed pro rata among all of the creditors and claimants. No provision is made in the National Banking Laws for preferred claims. The Courts have, however, established a basis for preferred claims where the claimant can show that the Receiver has, among the assets, identifiable property belonging to the claimant. In working out the formula or procedure for establishing such claims, the Federal Courts have held that the claimant must show, by the burden of proof, that from the transaction of the claimant with the bank before suspension the bank received property of the claimant in trust; that the property so received actually augmented the existing assets of the bank by way of adding thereto cash or other property (as distinguished from the addition of a bookkeeping credit); and that the

augmented assets, or the proceeds thereof, are traceable into the assets taken over by the Receiver. If for example a bank receives an item for collection and remittance under circumstances creating a trust relationship, and collection is made in the form of cash (as distinguished from the receipt in payment of a check drawn upon the bank) or if a bank receives cash funds in trust for a specific purpose, it is considered that the existing assets of the bank have been augmented or increased by the trust property, and consequently if it can be shown further that said trust property was not dissipated by the bank prior to suspension, but on the contrary the trust funds, or other funds constructively in lieu thereof, were retained by the bank and were taken over by the receiver at suspension, a preferred claim will be allowed. This rule is summarized in the decision of the Circuit Court of Appeals for the Eighth Circuit in *Empire State Surety Company v. Carroll County*, 194 Fed. 593, 603, 604, 606. In that case the bank had improperly received deposits and had fraudulently represented that it was solvent. In stating the applicable principles of law concerning preferred claims, the Court said:

> "This is a suit in equity against the Receiver of a National bank to require him to take from the ratable dividends of other creditors of the bank the requisite amount to pay the county's claim in full. The receiver must make the distribution of the property of this bank in accordance with the provisions of the National Banking Law. It is the dominant purpose and requirement of that law that, after provision for a redemption of its notes is made, the proceeds of an insolvent National bank shall be equally distributed among its unsecured creditors. So imperative is this provision that it repeals a former act of Congress giving a preference to the United States and annuls a statute of a state giving a preference to deposits of savings banks. *Rev. St. sec. 5236* (U. S. Comp. St. 1901, p. 3508); *Davis v. Elmira Savings Bank*, 161 U. S. 275, 285, 16 Sup. Ct. 502, 40 L. Ed. 700; *National Bank v. Colby*, 21 Wall. 609, 613, 614, 22 L. Ed. 687. The burden, therefore, is

on the sureties to prove clearly that they are entitled on equitable principles to the preference they seek. They proved that the bank took the deposits of the county and of its other depositors in trust for them respectively. But this was not enough. They were also required to prove that these deposits or their proceeds, or a certain part of them, came to the hands of the Receiver, for he is liable to cestuis que trustent to pay trust funds in full only to the extent that he receives them.

* * * * * * * * *

"It is indispensable to the maintenance by a cestui que trust of a claim to preferential payment by a Receiver out of the proceeds of the estate of an insolvent that clear proof be made that the trust property or its proceeds went into a specific fund or into a specific identified piece of property which came to the hands of the Receiver, and then the claim can be sustained to that fund or property only and only to the extent that the trust property or its proceeds went into it. It is not sufficient to prove that the trust property or its proceeds went into the general assets of the insolvent estate and increased the amount and the value thereof which came to the hands of the Receiver.

* * * * * * * * *

"But checks of third persons on the bank with which they are deposited which are paid by crediting the bank and charging the drawers on its books fail to increase the cash in its possession and form no basis for a preferential payment to the depositor. *Beard v. Independent District of Pella City*, 88 Fed. 375, 382, 31 C. C. A. 562.

"Moreover, the deposit of checks of third persons which are credited to the depositor and used by the bank to pay its debts bring no money into its fund of cash and form no foundation for preferential payment to the depositor. *City Bank v. Blackmore*, 75 Fed. 771, 773, 21 C. C. A. 514."

To the same effect see:

Second Circuit:
American Can Company v. Williams, 178 Fed. 420.
Sixth Circuit:
Brennan v. Tillinghast, 201 Fed. 609, 612, 613.
Eighth Circuit:
Larabee Flour Mills v. First National Bank, 13 Fed. (2nd) 330, certiorari denied, 273 U. S. 727.
Beard v. Independent District of Pella City, 88 Fed. 375, 382, 383.
Hirning v. Federal Reserve Bank, 52 Fed. (2nd) 382.
Ninth Circuit:
Titlow v. McCormick, 236 Fed. 209, 211, 212.
Tenth Circuit:
Blumenfeld v. Bank, 38 Fed. (2nd) 455.

Also see:

Schuyler v. Littlefield, 232 U. S. 707, 710, 713;
Cunningham, Trustee of Ponzi v. Brown, 265 U. S. 1, 11;
St. Louis & San Francisco R. R. v. Spiller, 274 U. S. 304, 310;
Blakey v. Brinson, 286 U. S. 254, 262, 263.

B. The Appropriation of a Deposit or Credit Balance Does not Result in Augmentation but Merely in a Shifting of Bookkeeping Credits.

The Federal Courts have held that the shifting or appropriation of a deposit or credit balance in a bank, whereby such shifted deposit or credit balance accrues to the bank, either as trustee or otherwise, contributes no additional assets, and creates no additional fund in the bank, and that consequently augmentation of existing assets does not occur. This situation frequently arises where an item has been forwarded to a bank for collection against one of its depositors, and the bank receives in trust in payment of the item a check of the debtor drawn upon his deposit account. In such case a charge is made to the debtor's deposit balance, and a corresponding credit, for remittance

purposes, is made in favor of the owner of the item. In such case no new funds accrue to the bank, and there has been merely a shifting of bookkeeping credits, and consequently there has been no augmentation. Under such circumstances a preferred claim cannot be allowed, according to the Federal decisions. In a recent case in the Eighth Circuit, *Hirning v. Federal Reserve Bank*, 52 Fed. (2nd) 382, 386, the Court, in discussing these principles, said:

> "It is contended by the appellee that the checks sent by the Reserve Bank to the Brookings Bank constituted a trust fund, and that this trust fund has been traced into the currency and collection items sent by the Brookings Bank to the Reserve Bank.
>
> "The trial court seems to have adopted this view as one of the grounds of its decision in ordering judgment for defendant.
>
> "*We do not agree with this contention.* It must be remembered that the checks sent to the Brookings Bank by the Reserve Bank were all of them checks drawn on the Brookings Bank. When the Brookings Bank accepted the checks, this produced no additional funds in its hands. Its assets were not augmented. *No trust fund was created. If there was no trust fund, there could, of course, be no tracing of the trust fund into any assets of the Brookings Bank.* The doctrine that a trust fund is created when checks drawn on bank A by a depositor therein are sent to bank A by bank B for collection, *i. e.*, for payment, has been disapproved by the decisions in this Circuit, as has also the doctrine that the forwarding bank or its principal has a general lien on the assets of the drawee bank for the payment of such checks. *Rorebeck v. Benedict, etc. Co.*, 26 Fed. (2) 440; *Farmers National Bank v. Pribble*, 15 Fed. (2) 175; *Larabee Flour Mills v. First National Bank*, 13 F. (2) 330; *Macy v. Roedenbeck*, 227 Fed. 346, 352; *Beard v. Independent Dist.*, 88 Fed. 375."

To the same effect are the cases in the various Circuits cited in paragraph A preceding.

In the instant case four items designated as (1) bank stock, (2) Graff note, (3) Sommer note, and (4) Veesaert

bonds, were received by the bank in trust. All of these items were disposed of by the bank prior to the appointment of the Receiver. In exchange for item 1 (the bank stock), the bank received no new assets but made a charge against a deposit balance in the bank to the credit of Cullinan (R. 50, 51). In exchange for item 2, the Graff note, the bank received no new assets but did receive its own certificates of deposit representing a charge against an existing deposit balance (R. 54), and the same is true of item 3, the Sommer note (R. 54). The claimant is a stranger to the transactions between the bank and Cullinan, Graff and Sommer from which the credit balances were built up in the names of these individuals, which credit balances were subsequently charged incident to the surrender of these three trust items. When the bank created a credit balance in favor of Cullinan based upon his note, Cullinan had the absolute right to draw and the bank became obligated to pay the deposit balance. Subsequent collections on the note were incident to the separate contract between Cullinan and the bank as to which the claimant is an absolute stranger. Thus prior to the surrender of the three trust items the relationship betwen the bank and Cullinan, Graff and Sommer had become that of debtor and creditor, hence the bank Receiver can be required to account for nothing but these transfers of credits as a general claim only. *Blakey v. Brinson*, 286 U. S. 254; *Allied Mills v. Horton*, 65 Fed. (2nd) 708; *Larabee Flour Mills v. First National Bank of Dublin*, 69 Fed. (2nd) 351; *City of Miami v. First National Bank*, 69 Fed. (2nd) 346; *Larabee Flour Mills v. First National Bank*, 13 Fed. (2nd) 330, certiorari denied, 273 U. S. 727; *Ellerbe v. Studebaker Corp.*, 21 Fed. (2nd) 993.

In principles the claimant in the instant case, as to the bank stock, Graff, and Sommer items, is in exactly the same position as was the preferred claimant in *Allied Mills, Inc. v. Horton*, recently decided by this Circuit Court of Appeals, reported in 65 Fed. (2nd) 708. In the Allied Mills

case the bank received an item, the property of the claimant, and surrendered it in exchange for transfers of credit already on its books, and the court properly classified the claim as general only. In the instant case the bank received the bank stock, the Graff and the Sommer items, as the property of the claimant, and surrendered them in exchange for transfers of credit already on its books, but the court allowed a preferred claim. An application of the principles stated in the following excerpts from the recent opinion of the court below in the Allied Mills case, pages 710 and 711, to the facts in the instant case, surrounding the bank stock, Graff and Sommer items, seems conclusively to classify the claim on these items as general only, and to exclude the claimant from any possible interest in the proceeds ultimately collected from Cullinan on his note and from any interest in the collection proceeds of the items deposited in the bank by Graff and Sommer to build up the credit balances, subsequently exchanged for the three trust items.

> "It is a rule of general application in Federal courts that where checks on the collecting bank are deposited in the same bank to meet a draft which the bank holds for collection, no trust in the funds thus deposited arises in favor of the drawer of the draft. *Hirning v. Federal Reserve Bank* (C. C. A. 8), 52 F. (2d) 382, 82 A. L. R. 297 change position of C. C. A. 8 to conform to other citations; *Larabee Flour Mills Co. v. First National Bank, of Dublin, et al.*, 52 Fed. (2nd) 146 (D. C.); *Larabee Flour Mills v. First National Bank of Henryetta, Okla.*, 13 Fed. (2nd) 330 (C. C. A. 8); *Empire State Surety Co. v. Carroll County, et al.*, 194 F. 593 (C. C. A. 8). The reason generally assigned in the cases is that in such transactions there is no augmentation of the assets of the bank. There is merely a transfer of existing assets of the bank from one to another.
>
> "If Crisp had brought into the bank the cash wherewith to pay this draft and had paid it in for that specific purpose, the assets of the bank would have been augmented by the cash thus brought in, and a trust

might then arise in favor of the drawer of the draft in case the bank fails to pay, and the funds coming into the bank are traceable.

* * * * * * * * *

"It is insisted that in any case the $105 of cash which Crisp deposited that day augmented the bank's assets by so much and should be held to constitute a trust. The instant this deposit was made the bank became debtor to Crisp, and the deposit became part of the bank's general assets. The fact that Crisp intended to use it to take up these sight drafts is immaterial. It may be presumed that one's checking account in a bank is intended sooner or later to be devoted to the uses of the depositor. This does not constitute such deposit a trust fund either for the benefit of the depositor or for such person or persons for whose use or benefit the depositor may intend to devote the account."

In exchange for item 4, the Veesaert bonds, the bank received a check in the amount of $1597.31, drawn on an outside bank which was passed to its credit with the First National Bank of Chicago. The record (P. 59) establishes that there was a subsequent low balance in this account of $643.24, the remainder having been dissipated through use by the bank in the payment of its debts. This subsequent dissipation limits the preferred claim accordingly, it being clear that any deposits in the account at Chicago after the low balance in question consisted of funds other than those of the claimant, for as stated by this Circuit Court of Appeals in its recent opinion in *Connolly v. Lang*, 68 Fed. (2nd) 199, 201:

"If the trust is once depleted, it can not be built up by subsequent deposits of other depositors. *Schuyler v. Littlefield, supra; Blumenfeld v. Union National Bank* (C. C. A.), 38 F. (2d) 455; *In re Brown* (C. C. A.), 193 F. 24."

C. There was no Valid Basis for Attempting to Impress the Cash in the Bank With a Trust in Favor of the Trustee in Bankruptcy Based Upon the Bank's Receipt and Subsequent Surrender of the Four Trust Items.

The Court below held that irrespective of the factor of tracing, the cash in the bank at the time the bank received the trust items or disposed of them was impressed with a trust in favor of the bankruptcy trustee to the extent of the value of the trust items, $8870.07, it appearing (R. 67, 68) that the cash on hand in the bank at all times thereafter until suspension exceeded this amount. This conclusion is erroneous because the record facts about which there is no dispute, clearly establish that not one penny of the proceeds of the four items held in trust went into the cash on hand in the bank.

It is the settled rule of the federal courts that the burden is upon the claimant for a preference to trace the proceeds of the trust property into the hands of the receiver, and that uncertainty or inability to show such tracing must result in denial. *Schuyler v. Littlefield, supra.* In this connection, this Court in its recent opinion in *Texas & Pacific Railway Co. v. Pottorff, Receiver*, 291 U. S. 245-261, said:

> "The claimant has the burden of identifying the property in its original or altered form. *Schuyler v. Littlefield*, 232 U. S. 707. It is not enough to show that at the time of receipt the general assets of the insolvent were increased or that debts were discharged."

In discussing a trust claimant's burden of proof incident to the tracing of proceeds of the transaction into the hands of the trustee of a bankruptcy estate this Court, in the opinion in *Schuyler v. Littlefield*, 232 U. S. 707-713, said:

> "All these claims were disallowed because of the failure to make the requisite proof. Our investigation of the facts leads us to the same conclusion so far as concerns the appellants' claim. They were practically

asserting title to $9,600 said to have been traced into stock in the possession of the Trustee. Like all other persons similarly situated, they were under the burden of proving their title. If they were unable to carry the burden of identifying the fund as representing the proceeds of their Interborough stock their claim must fail. If their evidence left the matter of identification in doubt the doubt must be resolved in favor of the Trustee, who represents all of the creditors of Brown & Co., some of whom appear to have suffered in the same way. Like them, the appellants must be remitted to the general fund."

The record in this case permits definite ascertainment of the disposition of the four items in question and their proceeds, and it clearly shows that none of these proceeds are traceable into the cash on hand in the bank that passed to the receiver at suspension. The only property passing into the hands of the bank receiver that contained any proceeds of the trust transaction was the balance he received from the First National Bank of Chicago, a correspondent bank, in connection with item No. 4 which contained the trust claimant's low balance of $643.24 (R. 59).

D. The Tracing of Funds Doctrine of Schumacher v. Harriett, 52 Fed. (2d) 817, Relied on by the Appellate Court for the Allowance of a Preferred Claim in the Instant Case is Erroneous Because in Conflict With the Decisions of This Court and Many Decisions of the United States Circuit Courts of Appeal.

In the Harriett case the bank received from the preferred claimant certain checks, representing the proceeds of life insurance, with instructions to purchase bonds with the proceeds, a trust transaction. The bank received credit for the checks in its accounts with Richmond and New York correspondents and, prior to suspension, dissipated the proceeds in payment of its debts. In allowing the preferred claim, the Appellate Court used the following lan-

guage in holding that the proceeds of the checks were traceable to the bank receiver (52 Fed. (2d) 819):

> "The life insurance checks were received by the bank as cash and were treated by it as such. They increased the cash and cash items in the tills of the bank at the time. When it placed them to its credit in the Richmond and New York banks, it was dealing with them as its own; and the presumption is that cash which was left in its tills was intended to be subject to the trust. While it had, of course, the right to collect the checks, it had no right to place their proceeds to its credit in other banks without holding an equivalent amount in cash in its own vaults to satisfy the trust which it had assumed towards plaintiff; and we must assume that it respected the trust, as 'equity imputes an intention to fulfill an obligation.'"

The facts in the Harriett case establish that none of the proceeds of the claimant's trust transaction passed into the hands of the bank receiver; hence the Circuit Court of Appeals should have classified the claim as general only. The case was a companion case to that of *Schumacher v. Brinson*, 52 Fed. (2d) 821, which was unanimously reversed by this Court as *Blakey v. Brinson*, 286 U. S. 254. The Harriett case is in conflict with the principles applied by this Court in the above excerpt from the opinion in *Schuyler v. Littlefield* and with its dictum, quoted above, in *Texas & Pacific Railway Co. v. Pottorff*, and with the principles established in *Blakey vs. Brinson*. This Court refused to review a contrary conclusion reached in *United States National Bank v. Centralia* 240 Fed. 93, certiorari denied 243 U. S. 656.

The tracing of funds principle in the Schumacher case stood alone until adopted by the Circuit Court of Appeals in the instant case and it has been repeatedly criticized. The annotator who prepared the exhaustive annotation in 82 A. L. R., beginning at Page 46, said on Page 203, in referring to this particular decision, that:

> "It is not altogether in harmony with the foregoing decisions."

The author of an article appearing in Volume 80, Pennsylvania Law Review, at Page 587, says, referring to the same decision:

> "It would seem that this decision would result in a recrudescence of the discredited doctrine which permitted a preference merely on proof that the assets had been increased by the trust property."

In the recent opinion of the Circuit Court of Appeals for the Fifth Circuit in *First National Bank, St. Petersburg v. City of Miami*, 69 Fed. (2d) 346, which was twice certified to this Court and the certificates dismissed on jurisdictional grounds, the Appellate Court discusses the "liberal" rules on tracing of funds but follows the settled federal rule and classifies the claim asserted as general only. The Court of Appeals for the Fifth Circuit declined to follow the Harriett tracing rule in its decision in *Pottorff v. Key*, 67 Fed. (2d) 833, and it comments adversely on the rule in its opinion in *Wisdom v. Keen*, 69 Fed. (2d) 349.

The Harriett tracing rule is in conflict with the rule stated by the Circuit Court of Appeals of the Eighth Circuit in one of the leading cases in this country on the question, that of *Empire State Surety Company v. Carroll County*, 194 Fed. 593, wherein the court requires, on Page 604, that:

> "Clear proof be made that the trust property or its proceeds went into a specific fund or into a specific identified piece of property which came into the hands of the receiver."

A review of the following cases will establish that the Harriett case stands as a solitary decision without support in the federal decisions, except in the instant case, and is opposed to the rule announced in every other Circuit of the United States. *American Can Co. v. Williams*, 178 F. 420, 422; *Commissioners of Crawford County v. Strawn*,

157 F. 49, 15 L. R. A. (N. S.) 1100; *Cuttell v. Fluent*, 51 F. (2d) 974; *Macy v. Roedenbeck*, 227 F. 346, 355; *First Nat. Bank v. Fidelity & Deposit Co.*, 48 F. (2d) 585; *Anadarko Cotton Oil Co. v. Litteer*, 300 F. 222; *Horse Co. v. Americus Nat. Bank*, 230 F. 738; *Banking Co. v. Fourth Nat. Bank*, 38 F. (2d) 772; *Sanders v. Stevens*, 51 F. (2d) 743; *Brennan v. Tillinghast*, 201 F. 609; *Gwynn v. Spurway*, 28 F. (2d) 37; *Dudley v. Richards*, 18 F. (2d) 876; *Titlow v. McCormick*, 236 F. 209; *Dickson v. First Nat. Bank*, 26 F. (2d) 411.

CONCLUSION.

It is believed that the foregoing discussion demonstrates that the decision of the Court below is contrary to the pertinent principles of law established in the Circuit Courts of Appeal in the Circuits other than Fourth and Seventh Circuits, and to the principles established by the decisions of this Court. It is earnestly urged, in the interest not only of uniformity in the administration of national banks throughout all of the Circuits, but also in the interest of settling conclusively what the law is upon the issues involved, that this Court entertain a review of this case on writ of certiorari, and we submit, in the light of the reasons indicated, that the petition should be granted.

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FILE COPY

Supreme Court of the United States

OCTOBER TERM, 1934.

No. 374.

ROSS C. ADAMS, Receiver of the Farmers National Bank of Pekin, Illinois, *Petitioner,*

vs.

EDWIN V. CHAMPION, Trustee in Bankruptcy of JOHN FITZGERALD, Bankrupt, *Respondent.*

BRIEF OF PETITIONER.

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SUBJECT INDEX.

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(A) Where as in the instant case, and in the companion cases Nos. 338 and 340, set for argument immediately before this case, a claimant seeks to recover from a Receiver of an insolvent National bank money alleged to have been held by the bank on a trust he must affirmatively establish, under the unmistakable trend and weight of Federal decisions: (1) that his transaction with the bank resulted in a trust relationship; (2) that the assets of the bank have been augmented or increased by new cash or property accruing from the claimant; (3) that the new property, in its original or changed form, can be traced to the assets taken over by the Receiver at suspension. No augmentation occurs, hence no tracing exists where the transaction results only in a shifting of bookkeeping credits on the books of the now insolvent National bank. In the instant case the now insolvent National bank received in trust an identifiable res in the form of the four items of collateral, consequently a trust relationship, at the outset, is admitted. The four collateral items were disposed of by the bank prior to its suspension. In exchange for the first three items the bank received nothing but transfers of credit already on its books which did not augment its assets and does not permit trac-

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ing of the proceeds to the Receiver. In exchange for the fourth item the bank received a check on an outside bank, which augmented its assets, but dissipated the proceeds thereof, prior to suspension, except as to the sum of $776.57 (admitted off the record, p. 18 ante). The respondent can establish a trust relationship, augmentation and tracing of funds as to the sum of $776.57 only, which sum should be fixed as the amount of the priority claim rather than the sum of $8,870.07 erroneously fixed by the Circuit Court of Appeals 7

(B) The tracing of funds principle of the Harriett decision, *supra*, relied on by the Circuit Court of Appeals for its allowance of this trust claim in the amount of $8,870.07 is erroneous because in clear conflict with the correct rule established by the weight of authority consisting of the decisions of this Honorable Court and the decisions of many Circuit Courts of Appeal 18 20

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BRIEF OF PETITIONER.

I.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals for the Seventh Circuit (Sparks, Circuit Judge) is reported in 70 Fed. (2nd) 956 and appears in the record at pages 82 to 87. The opinion of the United States District Court, Southern District of Illinois, Northern Division (Fitzhenry, D. J.) is unreported but its findings of fact, conclusions of law and decree appear in the record at pages 66 to 70.

II.

JURISDICTION.

Writ of certiorari was granted October 22, 1934 (R. 121) under Section 240 (a) of the Judicial Code as amended by the act of February 13, 1925 (U. S. C. Title 28, Section 347).

III.

STATEMENT OF CASE.

The Farmers National Bank of Pekin, Illinois, was found insolvent on January 8, 1932, and placed in the hands of a Receiver, appointed by the Comptroller of the Currency, for liquidation (R. 35). Thereafter, on June 24, 1932, in an action wherein the bank Receiver was not a party, a decree was entered by the District Court of the United States for the Southern District of Illinois Northern Division (R. 27, 30), adjudging that this bank had received an illegal preference from John Fitzgerald, a bankrupt, incident to the bank's receipt, prior to its suspension, of additional collateral for the Fitzgerald indebtedness, and directing the surrender of the collateral to the trustee in bankruptcy, plus payment of cash in lieu of four items of the collateral which were disposed of by the bank prior to its suspension. The bank Receiver complied with the decree by surrendering all of the bankrupt's collateral that passed into his hands (R. 37) but contested that part of the decree requiring the payment of the sum of $8,870.07, representing the value of four items of the bankrupt's collateral disposed of by the bank prior to suspension, on the ground that this claim was general only (R. 38). After a hearing on petition (R. 31 to 38), answer (R. 40 to 43), amendment to answer (R. 44 to 47) and stipulation of all facts (R. 48 to 60), the trial court held (R. 66 to 69) that the bank received the four items in question as trustee; that they were converted into cash by the bank; and by a decree entered July 7, 1933 (R. 69, 70) allowed the bankruptcy trus-

tee a priority claim of $8,870.07 against the bank Receiver. The Appellate Court affirmed the judgment of the District Court, 70 Fed. (2nd) 956 (R. 82 to 87). The bank Receiver's petition for rehearing was denied June 13, 1934 (R. 113).

The record is voluminous and somewhat confusing. *The issue is whether the proceeds of the four items of the bankrupt's collateral, admittedly received by the bank in trust, and disposed of by it prior to suspension, are traceable into the hands of the bank Receiver.* The pertinent record facts are as follows:

ITEM 1. This item consisted of ten shares of the capital stock of this now insolvent National bank, received by the bank as additional collateral for the bankrupt's indebtedness, and sold by it on February 9, 1929, to R. A. Cullinan for the sum of $3,000, *payment being effected by a charge against Mr. Cullinan's credit balance in the now insolvent National bank.* (R. 49-50) A portion of the priority claim allowed by the court below as to this item consisted of a $30 dividend on this stock *representing a debt due the shareholder by the bank.* (R. 49.)

ITEM 2. This item consisted of the Charles Graff note in the total amount of $3,183.78 received by the bank as additional collateral for the bankrupt's indebtedness, *and paid by Mr. Graff on April 12, 1929, by a charge against his deposit balance in this now insolvent National bank.* When Mr. Graff's deposit balance was charged on April 12, 1929, and the note delivered to him, two certificates of deposit, marked "Chas. Graff", representing the proceeds, were issued by the bank to its vice-president Reise whose representative later endorsed the same to the bank receiver. (R. 50 to 53, 61 to 62.)

ITEM 3. This item consisted of the W. C. Sommer note in the total amount of $1,059.98 received by the bank as additional collateral for the bankrupt's indebtedness *and paid by Mr. Sommer on April 16, 1929, by a charge against his deposit balance in the now insolvent National bank.* When

Mr. Sommer's deposit balance was charged on April 16, 1929, and the note delivered to him, two certificates of deposit, marked "W. C. Sommer," representing the proceeds, were issued by the bank to its vice-president Reise whose representative later endorsed the same to the bank receiver. (R. 53, 54, 62, 63.)

ITEM 4. This item consisted of five Veesaert mortgage bonds received by the bank as additional collateral for the bankrupt's indebtedness, and later involved in certain foreclosure proceedings in the course of which the now insolvent National bank surrendered said bonds and received a check in the sum of $1,597.31, drawn on the Edwardsville National Bank & Trust Company, *the proceeds of which passed to the credit of the now insolvent National bank with its correspondent*, the First National Bank of Chicago, on December 13, 1930. (R. 58.) The record, page 58, reflects that the total credit balance of the now insolvent National bank with the First National Bank of Chicago was $643.24 on October 27, 1931, which amount in changed form, is now traceable into the collateral surrendered by the Chicago bank to the Receiver (R. 59, 60). The bank Receiver admits, off the record (p. 18 [illegible]) that the low balance of his bank with the Chicago bank between December 13, 1930, and suspension was $776.57 as of December 28, 1931, which low balance is traceable to the Receiver. The low balance of $643.24 referred to in the record (p. 58) appears to have been erroneously taken from the books of the now insolvent National bank rather than from the books of the Chicago bank.

In answering the action of the bankruptcy trustee to establish a priority claim for the proceeds of these four items, the bank Receiver admitted that a general claim exists but defended against the priority claim on the ground that the bank's assets which passed into his hands were not augmented incident to the disposition thereof by the bank (R. 40 to 47). The District Court held that the four items of collateral were received by the bank in trust, converted

by it into cash, and decreed that payment of the full amount of $8,870.07 be made, subject to the rights of any other priority claimant, out of the sum of $30,548.61, the lowest amount of cash and cash items in the now insolvent National bank from February 5, 1929, to suspension. (R. 66, 69.) The Circuit Court of Appeals held "that the bank's assets were augmented by, and to the extent of the proceeds of the collateral and that those proceeds have, in law, been traced into the Receiver's hands" (R. 87), relying largely upon the tracing of funds rule of Schumacher v. Harriett, 52 Fed. (2nd) 817.

IV.

SPECIFICATION OF ERRORS.

(a) The Circuit Court of Appeals erred in holding, *in view of the record facts,* that any of the proceeds of the four items once held by the bank in trust, have, in law, been traced into the Receiver's hands.

(b) The Circuit Court of Appeals erred in not reversing the trial court's findings that the cash and cash items of the now insolvent National bank were impressed with a trust in any amount in favor of the respondent.

(c) The Circuit Court of Appeals erred in not classifying the respondent's entire claim as general only.

(d) The Circuit Court of Appeals erred in adopting and applying the tracing of funds rule of Schumacher v. Harriett, *supra,* to any of the collateral items because this rule is in conflict with the decisions of this Honorable Court and with the decisions of many Circuit Courts of Appeal.

V.

SUMMARY OF ARGUMENT.

(A) Where, as in the instant case, a claimant seeks to recover from a Receiver of an insolvent National bank money alleged to have been held by the bank on a trust, he must affirmatively establish, under the unmistakable trend

and weight of Federal decisions: (1) that his transaction with the bank resulted in a trust relationship; (2) that the assets of the bank have been augmented or increased by new cash or property accruing from the claimant; (3) that the new property, in its original or changed form, can be traced to the assets taken over by the Receiver at suspension. No augmentation occurs, hence no tracing exists where the transaction results only in a shifting of bookkeeping credits on the books of the now insolvent National bank.

In the instant case the now insolvent National bank received in trust an identifiable res in the form of the four items of collateral, consequently a trust relationship, *at the outset,* is admitted. The four collateral items were disposed of by the bank prior to its suspension. In exchange for the first three items the bank received nothing but transfers of credit already on its books which did not augment its assets and does not permit tracing of the proceeds to the Receiver. In exchange for the fourth item the bank received a check on an outside bank, which augmented its assets, but dissipated the proceeds thereof, prior to suspension, except as to the sum of $643.24 (according to the record). The respondent can establish a trust relationship, augmentation and tracing of funds as to the sum of $776.57 only (based upon the bank receiver's admission off the record (~~ante~~, p. 18), which sum should be fixed as the amount of the priority claim rather than the sum of $8,870.07 erroneously fixed by the Circuit Court of Appeals.

(B) The tracing of funds principle of the Harriett decision, supra, relied on by the Circuit Court of Appeals for its allowance of this trust claim in the amount of $8,870.07 is erroneous because in clear conflict with the correct rule established by the weight of authority consisting of the decisions of this Honorable Court and the decisions of many Circuit Courts of Appeal.

VI.

ARGUMENT.

(A) Where, as in the instant case, and in the companion cases Nos. 338 and 340, set for argument immediately before this case, a claimant seeks to recover from a Receiver of an insolvent National bank money alleged to have been held by the bank on a trust he must affirmatively establish, under the unmistakable trend and weight of Federal decisions: (1) that his transaction with the bank resulted in a trust relationship; (2) that the assets of the bank have been augmented or increased by new cash or property accruing from the claimant; (3) that the new property, in its original or changed form, can be traced to the assets taken over by the Receiver at suspension. No augmentation occurs, hence no tracing exists where the transaction results only in a shifting of bookkeeping credits on the books of the now insolvent National bank.

In the instant case the now insolvent National bank received in trust an identifiable res in the form of the four items of collateral, consequently a trust relationship, at the outset, is admitted. The four collateral items were disposed of by the bank prior to its suspension. In exchange for the first three items the bank received nothing but transfers of credit already on its books which did not augment its assets and does not permit tracing of the proceeds to the Receiver. In exchange for the fourth item the bank received a check on an outside bank, which augmented its assets, but dissipated the proceeds thereof, prior to suspension, except as to the sum of $776.57 (admitted off the record, p. 18, ~~ante~~). The respondent can establish a trust relationship, augmentation and tracing of funds as to the sum of $776.57 only, which sum should be fixed as the amount of the priority claim rather than the sum of $8,870.07 erroneously fixed by the Circuit Court of Appeals.

The mandate of the National Bank Act requires a pro rata distribution of the assets of an insolvent National bank among all creditors. This mandate can be avoided by the respondent only upon affirmative proof of trust relationship, augmentation, and tracing of funds to the Receiver.

Section 5236 U. S. R. S. (12 U. S. C. Ch. 2, Sec. 194) (Appendix p. 33), requires a pro rata distribution of an insolvent National bank's assets among all its creditors. In referring to this section this court said in Cook County National Bank v. United States, 107 U. S. 445, 450, that it

> "*provides for the distribution of the entire assets of the bank,* giving no preference to any claim except for moneys to reimburse the United States for advances in redeeming the notes. When this reimbursement is fully provided for, the balance of the assets, as the proceeds are received, is subject to a ratable dividend on all claims proved to the satisfaction of the receiver, or adjudicated by a court of competent jurisdiction."

Even the United States as a sovereign is a general creditor only, unless it has taken the security provided by law, except for advances to redeem circulating notes and in minor instances involving certified checks given for customs duties and certain taxes. (19 U. S. C. Ch. 3, Sec. 198; 26 U. S. C. Ch. 3, Sec. 109). The circulating notes are required to be adequately secured at all times and the debtor continues to be primarily liable for the taxes and duties, consequently the exceptions are very rarely applicable.

The respondent and all others similarly situated can avoid participation in the pro rata distribution provided by the National Bank Act only upon a showing that the assets that passed into the hands of the Receiver for the benefit of all creditors included the property of the claimant or its proceeds. The respondent must show, *by the burden of proof,* that as a result of the transaction the bank, before suspension (a) received property of the claimant in trust, (b) that the property so received actually augmented the existing assets of the bank by way of add-

ing thereto cash or other property (as distinguished from the addition of a bookkeeping credit) and (c) that the augmented assets, in their original or changed form passed into the hands of the Receiver.

Unless the record contains affirmative proof by the respondent of trust relationship, augmentation and tracing of funds to the Receiver the trust claim fails because all doubts must be resolved in favor of the bank Receiver who is the trustee for general creditors. As stated by this court in Texas & Pacific Railway v. Pottorff, 291 U. S. 245, 261 (note 19), decided at the last term:

> "The claimant has the burden of identifying the property in its original or changed form. Schuyler v. Littlefield, 232 U. S. 707. It is not enough to show that at the time of receipt the general assets of the insolvent were increased or that debts were discharged. Wuerpel v. Trust Co., 238 Fed. 269, 272-3; Knauth v. Knight, 255 Fed. 677; State Bank of Winfield v. Alva Security Bank, 232 Fed. 847; In re See, 209 Fed. 172; In re Dorr, 196 Fed. 292; City Bank v. Blackmore, 75 Fed. 771; compare Railway v. Spiller, 274 U. S. 304, 311; Cunningham v. Brown, 265 U. S. 1."

In its opinion in Schuyler v. Littlefield, 232 U. S. 707, this court said, at page 713:

> "All these claims were disallowed because of the failure to make the requisite proof. Our investigation of the facts leads us to the same conclusion so far as concerns the appellants' claim. They were practically asserting title to $9600 said to have been traced into stock in the possession of the Trustee. Like all other persons similarly situated, they were under the burden of proving their title. If they were unable to carry the burden of identifying the fund as representing the proceeds of their Interborough stock their claim must fail. If their evidence left the matter of identification in doubt the doubt must be resolved in favor of the Trustee, who represents all of the creditors of Brown & Co., some of whom appear to have suffered in the same way. Like them, the appellants must be remitted to the general fund."

The following excerpt from the opinion of the Circuit Court of Appeals of the Eighth Circuit in Farmers National Bank v. Pribble, 15 Fed. (2nd) 175, 176 summarizes the principles of law applicable to these trust claims:

> "It is clear that counsel for the plaintiff were familiar with and probably had before them when they drew this complaint *the established rule in the federal courts* prescribing the facts requisite to establish a cause of action by a cestui que trust to recover from the receiver of the property of an insolvent corporation the payment in full of a trust fund in his possession in preference to the payment of anything to its general creditors, for they pleaded and set forth such facts in the complaint as stated a perfect cause of action in accordance with that rule, which is:
>
> 'It is indispensable to the maintenance by a cestui que trust of a claim to preferential payment (by a receiver) out of the proceeds of the estate of an insolvent that clear proof be made that the trust property or its proceeds went into a specific fund or into a specific identified piece of property which came to the hands of the receiver, and then the claim can be sustained to that fund or property only, and only to the extent that the trust property or its proceeds went into it. It is not sufficient to prove that the trust property or its proceeds went into the general assets of the insolvent estate and increased the amount and value thereof which came to the hands of the receiver.' Empire State Surety Co. v. Carroll County, 194 F. 593, 114 C. C. A. 435, and cases there cited; Beard v. Independent School District, 88 F. 375, 31 C. C. A. 562; In re Seven Corners Bank, 58 Minn. 5, 59 N. W. 633; American Can Co. v. Williams (C. C.), 176 F. 816; Willoughby v. Weinberger, 15 Okl. 226, 79 P. 777; Macy v. Roedenbeck, 227 F. 347, 356, 142 C. C. A. 42, L. R. A. 1916C, 12; Central Trust Co. v. Chicago, A. & N. Ry. Co. (D. C.), 232 F. 936, 943; State Bank v. Alva Security Bank, 232 F. 847, 849, 147 C. C. A. 41; Titlow v. McCormick, 236 F. 209, 149 C. C. A. 399; Zenor v. McFarlin, 238 F. 721, 725, 151 C. C. A. 571; Scullin Steel Co. v. North American Co., 255 F. 945, 947, 167 C. C. A.

237; Mechanics & Metals Nat. Bank v. Buchanan (C. C. A.), 12 F. (2nd) 891.

The doctrine that a cestui que trust, whose property had helped to swell the general assets of a corporation which was or became insolvent, has a prior right to or interest in those general assets, without specific identification and tracing of such claimant's property, was again expressly repudiated by this court in the case last cited. The fact that the claimant's property paid or reduced the indebtedness or liability of the insolvent corporation, so that it will pay a larger percentage of its debts, justifies no lien on its assets by or preference in payment to the cestui que trust (1) because such a reduction of indebtedness does not increase the property or the value of the property of the insolvent; and (2) because the property of the claimant so used to pay a part of the insolvent's general indebtedness or liability never goes into, and therefore cannot be traced into, the property or assets of the insolvent which subsequently come into the possession of the receiver. Titlow v. McCormick, 236 F. 209, 149 C. C. A. 399; American Can Co. v. Williams (C. C.), 176 F. 816; Lucas County v. Jamison (C. C.), 170 F. 338; Multnomah v. Oregon National Bank (C. C.), 61 F. 912; Beard v. Independent School District, 88 F. 375, 31 C. C. A. 562; Hecker-Jones-Jewell Mill Co. v. Cosmopolitan Trust Co., 242 Mass. 181, 136 N. E. 333, 24 A. L. R. 1148." (Italics inserted)

The record establishes that in exchange for the first three items of the bankrupt's collateral valued at $7,272.76, the bank received nothing but transfers of credits already on its books. That such bookkeeping transfers did not augment the bank's assets and do not permit tracing to the Receiver is well settled by a long line of Federal decisions. *The trust res ceased to exist as to these three items when they passed out of the bank's possession in exchange for bookkeeping credits* because "an obligor cannot be trustee either of his duties or of the obligee's right under the obligation." American Law Institute, Trusts Restatement Section 75, and comment "a" and illustration thereto. As

stated by this court in Blakey v. Brinson, 286 U. S. 254, 263, in discussing similar transfers of credit "the cancellation of the credit balance by the debit neither suggests any intention to establish a trust, *nor points to any identifiable thing which could be the subject of it.*" (Italics inserted) In the recent opinion of the Circuit Court of Appeals for the Fourth Circuit in Edisto National Bank v. W. Raymond Bryant, Executor, 72 Fed. (2) 917, the court said:

> "*Trusts are not declared in vacuo because of a trust relationship. They must be predicated of particular property.* Blakey v. Brinson, 286 U. S. 254, 263; Texas & Pac. R. Co. v. Pottorff, 291 U. S. 245, 261; Swan v. Children's Home Society of West Virginia (C. C. A. 4th), 67 Fed. (2nd) 84, 87; Gulley v. Wisdom (C. C. A. 5th), 69 Fed. (2d) 495. And the record before us shows no property as to which a trust could have been predicated. *The failure of the bank to segregate funds or set aside securities may have been a breach of legal duty on its part, but it certainly resulted in no identifiable res which could be declared the subject of a trust.*" (Italics inserted)

The following excerpts from opinions of Circuit Courts of Appeal in check collection cases are applicable to the first three items paid by transfers of credits:

> Larabee Flour Mills v. First National Bank of Henryetta (C. C. A. 8), 13 Fed. (2nd) 330; 331; cert. den. 273 U. S. 727:
>
> "*The real issue in each case is between the preference claimant and general creditors of the bank. They will get less if the preference is allowed.* Each claimant asserted an equity that the assets taken over by the Comptroller are trust funds in which it is a preferred beneficiary. *It is difficult to explain or understand by what equitable right one who has not contributed to the creation of a fund should be given a special and superior interest therein, though some of the state courts seem to so hold.* The collecting banks acted as agents, Commercial Bank v. Armstrong, 148 U. S. 50, 13 S. Ct.

533, 37 L. Ed. 363, and had they collected and retained the funds called for by the drafts, as was their duty on account of insolvency, the equities of claimants would be plain; but instead of doing so *they merely shifted credits on their books and records. No part of the funds in the banks when they failed was placed there by claimants or by any one for them. In each case the draft was paid by check on the insolvent. No additional funds were brought into the bank by either transaction.* If the drafts which they held for collection had been paid in currency or by check on some other bank, the insolvents' assets would have been increased that much when thereafter their remittance drafts were dishonored; and in that event equity would have regarded the collections as trust funds, followed them into the increased assets and, to the extent of the increase applied them first in discharge of these claims. *This is our conception of the rule and the reason for it, applied in the federal courts.* It has been repeatedly announced by this court." (Italics inserted)

Hirning v. Federal Reserve Bank of Minneapolis (C. C. A. 8th), 52 Fed. (2nd) 382, 386:

"It must be remembered that the checks sent to the Brookings Bank by the Reserve Bank were all of them checks drawn on the Brookings Bank. *When the Brookings Bank accepted the checks, this produced no additional funds in its hands. Its assets were not augmented. No trust fund was created. If there was no trust fund, there could, of course, be no tracing of the trust fund into any assets of the Brookings Bank.* The doctrine that a trust fund is created when checks drawn on bank A by bank B for collection, *i. e.*, for payment, has been disapproved by the decisions in this Circuit, *as has also the doctrine that the forwarding bank or its principal has a general lien on the assets of the drawee bank for the payment of such checks.* Rorebeck v. Benedict, etc. Co., 26 Fed. (2nd) 440; Farmers National Bank v. Pribble, 15 Fed. (2nd) 175; Larabee Flour Mills v. First Nat. Bank, 13 Fed. (2nd) 330; Macy v. Roedenbeck, 227 Fed. 346, 352; Beard v. Independent Dist., 88 Fed. 375." (Italics inserted)

Anheuser-Busch Brewing Association v. Clayton (C. C. A. 5th), 56 Fed. 759, 760:

"Accepting Morris' check in payment of his debt to appellant, and charging the amount of it on Morris' account by the bank, was but a shifting of its liability, whereby it became appellant's debtor, and assumed the obligation to pay to it the amount of the check less exchange. There is nothing to indicate that this amount was separated and kept unmingled with the bank's own money; but, on the contrary, it is conceded that it is undistinguishable from the mass of the bank's own money, and cannot be traced to and identified in the hands of the receiver. This being so, appellant has no better equity than the other creditors of the bank, and is entitled to no priority over them. It can only come in as a general creditor, * * *"

First National Bank of St. Petersburg v. City of Miami (C. C. A. 5), 69 Fed. (2nd) 346, 347:

"As proven, no sum whatever was collected and held for plaintiff by the St. Petersburg bank to which a trust could attach. In this state of the proof *to hold the bank as trustee would be to hold it a trustee not of a thing, but of a claim against itself, a holding on its face so artificial and unreal as to be impossible.*" (Italics inserted)

It thus appears that the claim of the bankruptcy trustee, based upon the first three items of the bankrupt's collateral, is general only, because the bank, prior to suspension, received in exchange therefor nothing but bookkeeping credits for which the bank Receiver has always been ready to account by accepting a general claim.

The record indicates that the respondent may contend that it has the right to look behind the credit balances the bank received in exchange for collateral items 1, 2 and 3 (bank stock, Graff note, and Sommer note) and claim as the proceeds of the trust property what the bank received to build up these credit balances. It is the position of the

bank Receiver that the respondent must look to these credit balances exclusively and that he is a stranger to the separate transactions between the bank and its customers which resulted in credit balances in favor of Cullinan, Graff and Sommer. The Cullinan credit balance was built up by a loan from the bank (R. 49) which brought no new money into the bank and the respondent is a stranger to the subsequent payment of the loan, based upon a separate contract between Cullinan and the bank. Even though the note was not collected the bank would be required to account. The Graff credit balance was built up from a deposit of checks totaling $14,013.64 on April 12, 1929. The proceeds of this deposit are traceable (1) into the First National Bank of Peoria, Illinois, low balance thereafter $51.41 (R. 50); (2) into the First National Bank of Chicago, low balance thereafter $70.54 (R. 51) and (3) into a bank subsequently merged with the Commercial National Bank & Trust Company of Peoria, low balance thereafter $351.94 (R. 52). The record contains no affirmative proof that the bank Receiver ultimately received anything from these correspondent banks, except that the low balance of $70.54, traceable into the First National Bank of Chicago, is included in the sum of $776.57 admittedly due the respondent as traceable funds under collateral item No. 4, which will be discussed later. The Sommer credit balance, charged April 16, 1929, *was built up on March 27, 1929* (R. 55) by a transfer of a credit balance already on the bank's books in the name of T. M. Smith. The Smith credit balance was built up (R. 55, 56) by a prior deposit of checks totaling $14,308.10. The proceeds are traceable into the low balances of $51.41 and $351.94 with the Peoria banks, already referred to under the Graff item. However, as the record does not contain affirmative proof that the bank Receiver ultimately received anything from these correspondent banks even though all of these facts were material, no affirmative tracing appears, hence the claim is general only under the rule applied by this court in Schuyler v. Littlefield, 232 U. S. 707, 713.

The rule applied by the Federal courts where a trust claimant seeks to look behind the credit balance is summarized in the following excerpt from the recent opinion of the court below in Allied Mills v. Horton, 65 Fed. (2nd) 708, 710:

> "The fact that a considerable part of the funds wherewith the drafts were paid was deposited in the bank on the very day the draft arrived and was paid, is not material. Had the funds been on deposit in Crisp's account for weeks or months the incongruity would not appear. *Whether the interval is a matter of minutes or of weeks, the fact is that the funds were on deposit in the bank when Crisp drew his check in payment of the draft and received the bill of lading, and the relation of debtor and creditor then actually existed between them.*
> Through the transaction the bank received nothing. Crisp's check depleted his own account in the bank, and the bank's liability for the same amount to the drawer of the draft at once attached. No cash came to the bank. Nothing was taken from or added to its assets. It is insisted that in any case the $105 of cash which Crisp deposited that day augmented the bank's assets by so much and should be held to constitute a trust. The instant this deposit was made the bank became debtor to Crisp and the deposit became part of the bank's general assets. The fact that Crisp intended to use it to take up these sight drafts is immaterial. *It may be presumed that one's checking account in a bank is intended sooner or later to be devoted to the uses of the depositor. This does not constitute such deposit a trust fund either for the benefit of the depositor or for such person or persons for whose use or benefit the depositor may intend to devote the account.*" (Italics inserted)

In Blakey v. Brinson, 286 U. S. 254, a bank depositor built up his credit balance for the special purpose of purchasing bonds. This court held that after such deposits, even for the purpose intended, the relationship between the

bank and the depositor was that of debtor and creditor, and denied the trust claim asserted. The same result was reached by the Circuit Court of Appeals for the Fifth Circuit in Larabee Flour Mills v. First National Bank of Dublin, 69 Fed. (2nd) 351, where the court said:

> "We notice only to reject a contention that Street & Co. on September 20 deposited in the Dublin bank checks drawn on other banks for the purpose of providing a special fund to meet its check given on that day to take up appellant's draft, because it appears that in making those deposits Street & Co. used the customary form of deposit slip, and, 'in accordance with its instructions, the deposit was credited by the bank in the usual manner.' After those deposits, 'as before, the bank remained a debtor' and Street & Co. 'a creditor for the amount of the credit balance.' Blakey v. Brinson, 286 U. S. 254, 52 S. Ct. 516, 517, 76 L. Ed. 1089, 82 A. L. R. 1288."

It thus appears that the respondent cannot look through the credit balances the bank received in exchange for the bank stock, Graff and Sommer items, hence that the facts concerning the building up of these credit balances are immaterial in determining the status of the respondent's claim.

For item 4 of the bankrupt's collateral, the 5 Veesaert mortgage bonds, the bank received a check in the amount of $1,597.31 drawn on an outside bank, the proceeds of which are traceable into its deposit balance with the First National Bank of Chicago as of December 13, 1930 (R. 58). The record, at page 58, evidences that the total credit balance of the now insolvent National Bank with the First National Bank of Chicago on October 27, 1931, was $643.24. The record does not contain affirmative proof that the now insolvent National bank's balance with the Chicago bank was at least $643.24 at all times between December 13, 1930, and October 27, 1931, and between October 27, 1931, and suspension on January 7, 1932. Consequently, if the

respondent is limited to the record, no part of these proceeds are traceable to the bank Receiver under the rule applied by this court in Schuyler v. Littlefield, 232 U. S. 707, 713, which classifies the entire trust claim of $8,870.07, as general only. However, since the decision of the court below in this case, the Comptroller of the Currency has obtained from the books of the First National Bank of Chicago, certified by it to be correct, a transcript of the account of the Farmers National Bank of Pekin, which evidences that the now insolvent National bank's balance with this Chicago bank was in excess of the sum of $1,597.31 at all times between December 13, 1930, and suspension except that the total balance on December 28, 1931, was $776.57.

The court below found (R. 84) that the least amount in cash and cash items on hand in the now insolvent National bank during the period from February 5, 1929, to the close of business on January 7, 1932, was $30,548.61. We know, however, from the record facts already discussed, that not one dollar of the proceeds of the four items of collateral are traceable into the cash or cash items on hand in the bank. Three of the items were exchanged for transfers of bookkeeping credits and the fourth for a check the proceeds of which were passed to the now insolvent National bank's credit in a Chicago bank. The collateral returned to the bank Receiver, after suspension was impressed with a trust in the amount of $776.57 in favor of the respondent but *no basis exists for the conclusion of the court below that any part of the proceeds of the bankrupt's collateral are traceable into the cash or cash items on hand in the bank at suspension.*

In the absence of a segregation, trust relationship as to the first three items of collateral failed when they were surrendered by the bank. As said by Mr. Justice Stone in an article entitled "Legal Problems in the Transmission of Funds", Columbia Law Review, June, 1921;

Page 518: "Even if there were an executory undertaking of the bank to become a fiduciary by setting apart such specific sum, such a relationship is not established until there is some actual setting apart or segregation of the money, or some other res as the subject matter of the fiduciary relationship."

Page 525: "The very essence of the right of priority over other creditors depends upon the setting apart of a particular fund for the benefit of the depositor. There is no basis for giving one depositor a priority over another unless this is an essential part of the transaction."

The difference between segregation and non-segregation is illustrated in St. Augustine Paint Company v. McNair (C. C. A. 5) 59 Fed. (2nd) 755, where the bank physically segregated a part of its cash to purchase the claimant's check held for collection. The court in its opinion at page 757 said:

> "*The conversion of the check into cash and segregation of such cash from the bank's general assets before using the check are of vital consequence, as those facts distinguish that transaction from those in which a bank of deposit merely credited a check to the depositor's account so as to become the depositor's debtor,* and thereafter used the check to pay the bank's own debts in such a manner that the proceeds were absorbed in a clearing transaction with no gain to the receiver, such as in Empire State Surety Co. v. Carroll Co. (C. C. A. 8) 194 Fed. 593, and other cases cited."
> (Italics inserted)

To summarize, the Farmers National Bank of Pekin received in trust four items of collateral, the property of John Fitzgerald, a bankrupt. Prior to its suspension the bank exchanged three of these items (bank stock, Graff note and Sommer note) for bookkeeping credits already on its books which classifies the bankruptcy trustee's claim as general only to this extent. In exchange for the fourth item

of collateral (the Veesaert mortgage bonds) the now insolvent National bank received a credit in the amount of $1597.31 in a correspondent bank. The record contains no affirmative proof that any part of this correspondent bank credit ever passed into the hands of the bank Receiver, consequently, on the record, the entire trust claim of $8870.07 is general only because of the failure to trace any proceeds into the hands of the bank Receiver. If the record can be read in the light of the supplemental information furnished herein by the Comptroller of the Currency, the respondent can trace the proceeds of item 4, the Veesaert mortgage bonds, to the extent of the sum of $776.57 only, the low balance in the First National Bank of Chicago as of December 28, 1931, which gives him the right to a trust claim in this amount, subject to possible prorating with other trust claimants similarly situated, and a general claim only for the balance.

(B) The tracing of funds principle of the Harriett decision, supra, relied on by the Circuit Court of Appeals for its allowance of this trust claim in the amount of $8870.07 is erroneous because in clear conflict with the correct rule established by the weight of authority consisting of the decisions of this Honorable Court and the decisions of many Circuit Courts of Appeal.

The tracing of funds theory of Schumacher v. Harriett, 52 Fed. (2nd) 817, accepted and applied by the court below in the instant case to allow the trust claim in full, is erroneous and is in conflict with the decisions of this court and many circuit courts of appeal.

In the instant case the court below made no attempt to specifically trace the proceeds of the four items of collateral into the hands of the bank Receiver but relied on the tracing fiction erroneously resorted to, we submit, by the Circuit Court of Appeals for the Fourth Circuit in Schumacher v. Harriett, 52 Fed. (2nd) 817. Consequently *the*

question in this connection presented in the instant case, is the soundness of the tracing of funds doctrine of the Harriett case. On this question the court below stated in its opinion (R. 85):

> *"It is further contended by appellant that the property in controversy has not been traced into his possession, which of course is necessary before appellee can recover.* In Schumacher v. Harriett, 52 Fed. (2nd) 817, it was disclosed that plaintiff had delivered life insurance checks to the bank to purchase bonds for plaintiff with the proceeds; that the checks were received by the bank as cash and treated by it as such, plaintiff receiving immediate credit therefor; that it forwarded the checks for credit to corresponding banks, in which on that day, and for several days thereafter, the sending bank had credit balances considerably in excess of the respective amounts so deposited. Those balances were gradually reduced until, *at the time of the depositing bank's failure, the account with one of the correspondent banks showed an overdraft, and the account with another bank showed a small balance which was credited upon a note which the correspondent bank held.* It was there said that the plaintiff, under those circumstances, had traced the trust fund in the bank receiver's hands." (Italics inserted)

The decisions of this court and the Circuit Courts of Appeal discussed under "A" above would necessarily, as a matter of principle, classify the trust claim asserted in the Harriett case as general only, because it clearly appears from the facts presented therein that the proceeds of the two checks received by the bank in trust, which augmented its assets, were completely dissipated by the bank prior to the time it passed into the hands of the Receiver. The decision in the Harriett case erroneously required the funds of the bank which belonged to the depositors to respond in full for the trust claim despite the fact that these funds were in no way enriched by the transaction. As hereinafter indicated (*infra* pp. ~~22-23~~ 26-28) this phase of the Harriett

decision has been repeatedly criticised and it stood alone in the Federal decisions until adopted by the court below in the instant case.

It is pure fiction to say, as was said by the courts below in the instant case and in Schumacher v. Harriett, that any part of the proceeds of the claimant's items, originally held by the banks in trust are traceable into the cash or cash items owned by the banks that passed into the hands of the Receiver. The tracing of the disposition of the items according to the record establishes, in each case, that not *one* dollar contained in the cash or cash items of the banks that passed to the Receiver was placed there by the trust claimants or any one on their behalf. The reasons why fiction should not be resorted to in establishing trust claims where the depositors of insolvent National banks are to be adversely affected are very well stated by the court below in its recent opinion in Connolly v. Lang, 68 Fed. (2d) 199, 202:

> "If this were a controversy only between appellee and the Bank there might be good reason for permitting fiction to pervert the facts because all the equities would be with appellee. This action, however, is really between appellee and the general depositors, who without fault on their part have been placed in positions which no doubt are equally deplorable and whose rights to have equity done are equally worthy of consideration."
>
> "From these facts and the further facts that the pass book was retained by the Bank and an entry made thereon showing that the entire amount had been drawn out and the ledger sheet pulled, appellee argues that it must be considered that she actually received possession of all the money and thereafter returned it to the bank officer, thereby augmenting the assets of the Bank. Of course, she never actually had the $8500 in her possession, and *we think we are not warranted in indulging in that fiction as between appellee and the other creditors.*" (Italics inserted)

In First National Bank of Ventura v. Williams, 15 Fed. (2nd) 585, 588, the Court said:

> "The answer to this is that courts must decide cases, not upon suppositions, but upon facts as proven or admitted, and the admitted fact is that cash was not received for the check, but that it was used merely to reduce the liabilities of the bank."

For expressions of opinions of other Appellate courts to the same effect we quote the following:

Wisdom v. Keen, (C. C. A. 5), 69 Fed. (2nd) 349, 350:

> "Equity if dealing with the bank alone might well consider that it had done what it should have done and might well hold it to the consequences. American National Bank v. Miller, 229 U. S. 517, 33 S. Ct. 883, 57 L. Ed. 1310. But in dealing with the distribution of the assets of an insolvent national bank and with the requirement of ratable dividends to all claimants a more stringent adherence to what was actually done is proper."

Beard v. Independent Dist. (C. C. A. 8), 88 Fed. 375, 381:

> "It is claimed in argument that the court must treat the case just as though the treasurer of the school district had presented the check, had obtained the money thereon, and had then deposited the money in the bank as the money of the school district, but this was not in fact done; and *as against the creditors, whose money in fact created the cash amount coming into the hands of the receiver, why should fiction be resorted to in order to sustain a preference on behalf of the school district to payment out of a fund not augmented in fact by any sum belonging to the district?*" (Italics inserted)

Smith v. Zemurray, (C. C. A. 5) 69 Fed. (2nd) 5, 6:

> "To the appellee's 'as if' argument, 'the matter is to be treated as though Robinson had presented the check to the teller and on receiving the money had paid it back over the counter to buy a draft,' American National Bank v. Miller, 229 U. S. 520, 33 S. Ct. 883, 57 L.

Ed. 1310, the receiver replies: 'Not so.' We know from Robinson's own testimony that this did not occur. *We know* from it that *what did occur* was an exchange of the paper of a bank, hopelessly insolvent, if plaintiff is right, in the form of an accepted draft on it, for paper of the same bank in the form of its draft on New York. This and nothing more.' He argues, too, that *when what actually occurred is known, it is idle to speculate on what might have been the legal effect of an entirely different occurrence.* Blakey v. Brinson, 286 U. S. 254, 52 S. Ct. 516, 76 L. Ed. 1089, 82 A. L. R. 1288." (Italics inserted)

Hecker-Jones-Jewell Milling Co. v. Cosmopolitan Trust Co. (Supreme Judicial Court of Mass.) (De Courcy, J.) 136 N. E. 333, 335:

"The other theory is that the transaction by which the draft was paid was in legal effect the same as if B. Greenglass & Son had drawn from their account through paying teller the sum of $3,518, in money, and then handed it back to the collecting teller in payment of the draft. But *that is not what the debtor did; and the difference is essential, not a mere matter of form. The payment made to the bank was not cash, to which the moment before it had not the slightest claim, and which therefore would count as wholly separate 'proceeds' of the collection; it was merely the lessening of one of its own debts, and productive of nothing even remotely suggesting a 'res' for a trust. The difference between the legal significance of the actual and the assumed courses of action cannot be ignored or confused.*" (Italics inserted)

People v. Merchants & Mechanics Bank, 78 N. Y. 269:

"The learned counsel contends that the Troy Bank was agent of the Chemical Bank to receive payment of the check. Suppose it were, *what did it receive as such payment? Simply its own obligation. If anything was set apart by charging up the check, it was only so much of the bank's indebtedness to its depositor.* * * * To make this case analogous it would be necessary to

show that the Troy Bank had separated from its general assets, and placed in the hands of some depositary, a sum sufficient to pay the check, for the express purpose of being so applied, and that this fund had come to the hands of the receiver in some form. There is no approach in this case to any such state of facts." (Italics inserted)

It should be noted that the case of Schumacher v. Harriett relied on by the court below for the allowance of this trust claim, was a companion case to that of Schumacher v. Brinson, 52 Fed. (2nd) 821. In both of these cases the court below relied on fictions to establish a trust against the assets of an insolvent National bank. Certiorari was applied for in the Brinson case only and the decision of the court below was unanimously reversed as Blakey v. Brinson, 286 U. S. 254. In disposing of the contention that a fiction contrary to the facts should be resorted to this court said, in its opinion at page 262:

"The court below thought that the legal consequence to be attributed to the debiting of the account with the supposed purchase price of the bonds was the same as if the respondent had cashed a check for the amount and had then proceeded to hand the money back to the bank under a specific agreement between him and the bank that the money was to be held as a special fund, for the sole purpose of completing the purchase. This view is not without support. (Citing authorities) *Such a procedure, if actually carried out, might afford a basis, which is lacking here, for the inference that respondent,* no longer content with the rule of creditor, *had sought to establish a trust fund. But the mere debiting of his account, without more, for the reimbursement of the bank for the obligation which it was supposed to have incurred or paid, lends no support to such an inference. The cancellation of the credit balance by the debit neither suggests any intention to establish a trust nor points to any identifiable thing which could be the subject of it.*" (Italics inserted)

Had the court below adhered, in the instant case, to the principles stated by it in denying similar trust claims in its recent opinions in Connolly v. Lang, 68 Fed. (2nd) 199, 202, and Allied Mills v. Horton, 65 Fed. (2nd) 708, 710, the Harriett tracing of funds fiction would have been rejected and the respondent's entire claim classified as general only.

The tracing of funds rule of the Harriett case is the basis of a number of actions now pending in the lower Federal courts to establish similar claims against Receivers of insolvent National banks. Some of these cases involve large amounts, two in excess of $300,000 each. If the Harriett tracing rule is sound outstanding trust claims based thereon will very substantially reduce the total dividends paid depositors of insolvent National banks.

The petitioner's contention concerning the unsoundness of the Harriett tracing of funds rule are summarized in the following excerpts from recent opinions of the United States Circuit Court of Appeals for the Fifth Circuit.

Pottorff v. Key, 67 Fed. (2nd) 833, 834:

> "Schumacher v. Harriett (C. C. A.), 52 Fed. (2nd) 817, 82 A. L. R. 1, is much relied on to sustain the judgment appealed from. The court there reviews the cases and concedes that they establish such principles as we have just asserted, but avoids their consequences by *the novel view* that a trust check, when treated by a bank as one of its cash items, is thereby confused with its cash as though it had been unidentifiable currency; and that, if the bank misuses the check, it thereby sets apart as a trust res an equivalent value of other cash assets. *Such a doctrine amounts to saying that in every case of misapplied money or money's equivalent the wrongdoer's other cash and cash items stand in its place so long as he has any, establishing in effect a general lien on all such. 'If the plaintiff's contention be well founded, and to follow misappropriated moneys it is only necessary to show that a receiver has, and that the trustee had, assets, the rule is simply that a demand for such moneys is a preferred claim against any substantial estate. To adopt this view is to do away with*

all the equitable principles out of which the right to follow trust funds grew.' American Can Co. v. Williams (C. C. A.), 178 F. 420, at page 423. *We hold in this connection that, if a trust res can be followed, it must be; and that a lien by confusion can be fixed on a fund only when the confusion is actual and when the fund is shown to have really received and to still contain the trust res or its proceeds.* The judgment is reversed, with direction to disallow appellee's claim as preferred and to allow it as a general claim only." (Italics inserted)

Wisdom v. Keen, 69 Fed. (2nd) 349, 350:

"The view that when a bank becomes obligated to collect for another person checks drawn on itself and makes entries of their collection, it must in equity be considered to have done what it should have done, to wit, to have collected them in cash though afterwards commingling the customer's cash thus collected with its own, so that a traceable res is brought into being with title vested in the customer, has been adopted by a growing number of state courts and is said to be the majority view in an elaborate examination of the cases in 82 A. L. R., page 97. *It was pressed to its furthest extent in the Fourth Circuit in Schumacher v. Harriett,* 52 Fed. (2nd) 817, 82 A. L. R. 1, and *Schumacher v. Brinson,* 52 Fed. (2nd) 821. *Otherwise the federal cases have been to the contrary.* 82 A. L. R. 101. Schumacher v. Brinson was appealed and reversed as Blakey v. Brinson, 286, U. S. 254, 52 S. Ct. 516, 76 L. Ed. 1089, 82 A. L. R. 1288. *We refused to follow Schumacher v. Harriett in Pottorff v. Key* (C. C. A.), 67 Fed. (2nd) 833. At the conclusion of the opinion in *Texas & Pacific R. Co. v. Pottorff,* 54 S. Ct. 416, 78 L. Ed. ——, *the Supreme Court again indicates the necessity of an identifiable trust res in order to create a trust by misconduct as distinguished from a general liability in contract or tort. Whether the question be one of general equity jurisprudence or of the application of the federal law relating to insolvent national banks, the views of the federal courts must in such courts be controlling."* (Italics inserted)

The same criticism of the Harriett opinion is made in 80 Pennsylvania Law Review 587.

Since its decision in Schumacher v. Harriett, 52 Fed. (2nd) 817, the Circuit Court of Appeals for the Fourth Circuit has not allowed a trust claim against the Receiver of an insolvent National bank except where the record contained affirmative proof of the three essentials of trust relationship, augmentation and specific tracing of the proceeds to the Receiver. The petitioner submits that since the decision of this Court in Blakey vs. Brinson, 286 U. S. 254, the recent well considered opinions of the Circuit Court of Appeals for the Fourth Circuit in this class of cases indicate its departure from the position taken in Schumaker vs. Harriett and to some extent in Ellerbe vs. Studebaker Corp., 21 F. (2) 993, and a return to or adoption of a position of strict adherence to the settled Federal rule requiring *actual* augmentation and tracing rather than fictions. We refer in this respect to the recent opinions of the Circuit Court of Appeals for the Fourth Circuit in Harmer v. Rendleman, 64 Fed. (2nd) 422; Swan v. Childrens Home Society, 67 Fed. (2nd) 84, certiorari denied 290 U. S. 704; Santee Timber Corp. v. Elliott, 70 Fed. (2nd) 179; Edisto National Bank of Orangeburg v. W. Raymond Bryant, Executor, 72 Fed. (2) 917, and Spradlin Receiver v. Royal Mfg. Co., as yet unreported, decided November 19, 1934. The petitioner believes that these latter opinions indicate that the Harriett claim would be classified as general only if represented to the Circuit Court of Appeals for the Fourth Circuit today.

The bank Receiver assumes that this court's action in granting a review disposes of the contention set out in the respondent's brief in opposition to the petition for writ of certiorari to the effect that this court will not review findings of fact in which both courts below concur. It is settled that this court will review findings of fact concurred in by the two lower courts when shown to be clearly against the

evidence or induced by an erroneous view of the law. Bodkin v. Edwards, 255 U. S. 221, 223; Texas & New Orleans Railroad Company v. Railway Clerks, 281 U. S. 548, 558. Applying the rule to the instant case it appears that the record before this court contains all the evidence that was before the courts below, the facts having been stipulated. The trial court found as a fact (R. 67) that the four items of the bankrupt's collateral "were converted into cash and used by the Receiver's bank as its own." This finding was clearly erroneous because the record establishes beyond any question that three of the four items of collateral were not converted into cash by the bank but were exchanged for transfers of bookkeeping credits. The trial court found that the proceeds of the four collateral items were traced into the cash and the cash items on hand in the bank at suspension. This was clearly erroneous because we know from the record, as already discussed, that not one dollar contained in the cash and cash items came from the four items of collateral. The bank Receiver denies that the trial court's findings of fact were concurred in by the Appellate court. On the contrary the Appellate court disagreed with the trial court's findings of fact when it held that the four items of collateral were not converted into cash in this language of its opinion (R. 85). "It is next contended by the appellant that the bank's assets were not augmented by the amounts received by it in payment of the obligations of the collateral. *This is no doubt true,* * * *" The Appellate court did not find, as a matter of fact, as was found by the District court, that any of the proceeds of the four items of collateral had been traced, *under the record,* to the Receiver. The Appellate court's conclusion is based upon a legal fiction as evidenced by the language in the opinion (R. 87): "We are convinced that the bank's assets were augmented by, and to the extent of, the proceeds of the collateral, and that those proceeds have in law been traced into the Receiver's hands." The bank Receiver submits

that this case does not present findings of fact concurred in by the two lower courts; that the case does present findings of fact by the trial court shown to be clearly erroneous by the stipulation of all facts contained in the record before this court, and that the clearly erroneous findings of fact and conclusions of law of both courts below should be reviewed as was done in the similar case of Blakey v. Brinson, 286 U. S. 254.

The National Banking Laws and related acts, together with a long line of decisions by this Court clearly evidence an intent to safeguard the assets of insolvent National banks in liquidation, thus insuring a maximum distribution to the depositors and creditors. Taxes due the United States which would be paid from the funds of depositors are abated. (Sec. 570, Title 12 U. S. C. A.) The preference given the United States as a sovereign against insolvent estates generally is inapplicable to such banks. Suits to wind up the affairs of such banks are made cognizable in the Federal courts, *independent of the amount involved.* A separate system of liquidation is provided, independent of the Bankruptcy Act. Sales and compromises of assets can be made only after court approval and advances to protect assets can be made only upon approval by the Secretary of the Treasury. Annual reports of the results of liquidation are required to be made to Congress. While the claimants in the instant case and in the companion cases Nos. 338 and 340 assert ownership of property taken over by the Receivers they are in fact, as established by the record, seeking to be made whole from the funds of the depositors. To permit any class of claimants to be paid in full from the funds of depositors, when such funds were in no way enriched by the claimants' transactions, would flagrantly violate the principles heretofore adhered to in liquidating insolvent National banks.

The depositors and other creditors of this insolvent National bank—the beneficial owners of its assets—will suffer a substantial loss because of their dealings with the bank.

Their equities are at least equal to those of the respondent. The four items of the bankrupt's collateral upon which this trust claim is based, were disposed of by the bank prior to suspension. The record establishes beyond any question the identity of the proceeds received by the bank. In exchange for the first three items the bank received nothing but pre-existing credit balances on its books which definitely defeats all prospect of tracing funds to the Receiver. The record does not contain affirmative proof that any part of the proceeds of the fourth item is traceable into the hands of the bank Receiver, consequently the entire claim is general only, under the record. If the additional information supplied by the Comptroller of the Currency can be considered the respondent should be allowed a priority claim in the amount of $776.57, subject to a possible pro rating with any other trust claimants similarly situated and a general claim only for the balance. This sum of $776.57 represents that part of the proceeds of the fourth item of collateral, traceable to the First National Bank of Chicago, that was not dissipated through use by the now insolvent National bank in payment of its debts prior to suspension.

VII.

CONCLUSION.

It is believed that the foregoing discussion establishes that the record shows that the cash and cash items of this insolvent National bank are not impressed with a trust in favor of the respondent, in any amount, as held by the court below; that all four of the bankrupt's items, held in trust by the bank, were disposed of by it prior to suspension; that in exchange for three of the items the bank received nothing but pre-existing credit balances on its books which result, to this extent, in a general claim only; that in exchange for the fourth item the bank received a check on an outside bank, the proceeds of which are not affirmatively traced, of record, to the bank Receiver, and consequently,

based on the record, the respondent's entire claim is general only. If the additional information furnished herein by the Comptroller can be considered by this court, the respondent should be allowed a priority claim in the amount of $776.57, which, as a matter of fact, represents the only proceeds of the bankrupt's collateral that passed into the hands of the bank Receiver after suspension. If a priority or preferred claim in the sum of $776.57 is allowed, we consider that the final decree in the case should direct the bank Receiver to certify any claim allowed, to the Comptroller of the Currency for payment in due course of administration, thus insuring that the rights of any other claimants similarly situated, who may have proved their claims to the satisfaction of the Comptroller as provided by Section 194, Title 12, U. S. C. A., will be protected.

It is submitted that the decision of the court below should be reversed.

Respectfully submitted,

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Of Counsel.

APPENDIX.

U. S. C. A. Title 12, Section 194:

DIVIDENDS ON ADJUSTED CLAIMS; DISTRIBUTION OF ASSETS. From time to time, after full provision has been first made for refunding to the United States any deficiency in redeeming the notes of such association, the Comptroller shall make a ratable dividend of the money so paid over to him by such receiver on all such claims as may have been proved to his satisfaction or adjudicated in a court of competent jurisdiction, and, as the proceeds of the assets of such association are paid over to him, shall make further dividends on all claims previously proved or adjudicated; and the remainder of the proceeds, if any, shall be paid over to the shareholders of such association, or their legal representatives in proportion to the stock by them respectively held. (R. S. 5236.)

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, A. D. 1934.

No. 374

ROSS C. ADAMS, Receiver of the Farmers National Bank of Pekin, Illinois,
Petitioner,

vs.

EDWIN V. CHAMPION, Trustee in Bankruptcy of John Fitzgerald, Bankrupt,
Respondent.

BRIEF ON BEHALF OF RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

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ARGUMENT.

A. Both the District Court and the Circuit Court of Appeals found the facts in the same way. Therefore, the facts in this Court are not open to question.

In accordance with Equity Rule 70½, the District Court made findings of fact as follows:

> "(1) The Court finds that these four items are those above set forth which aggregate the principal sum of $8870.07.

"(2) The Court further finds that the Bank of the Receiver received the four items of collateral above described (Graff Item $3183.78; Sommer Item $1058.96; Bank Stock Item $3030.00; Veesaert Item $1597.31) as an unlawful and recoverable preference; that the several elements were converted into cash and used by the Receiver's Bank as its own.

"(3) The Court further finds that the said several items are and were impressed with a trust for the benefit of the creditors of John Fitzgerald, Bankrupt.

"(4) The Court further finds that shortly after receiving the collaterals in question the defendant Bank converted them into cash and treated them as such and as its own.

"(5) The Court further finds that on January 7, 1932, when the said defendant Bank closed, it had on hand in cash and cash items $36,054.76, and that this fund afterwards went into the hands of the Receiver; that the least amount in cash and cash items in the defendant Bank during the period February 5, 1929, to the close of business on January 7, 1932, was $30,548.61; that the defendant Bank by collecting notes and bonds belonging to the plaintiff as Trustee in Bankruptcy, and the sale of ten shares of stock, without the knowledge or consent of the Trustee, held the proceeds of such collections and sale, amounting to $8870.07, as a Trustee *ex maleficio,* and that the said funds were in the funds on hand at the time of the closing of the Bank, and that plaintiff is entitled to have said claim for $8870.07 allowed as a priority." (R. p. 67).

Of the findings of the District Court, the Court of Appeals in its Opinion said:

> "The Court's findings which are material to the questions here presented are substantially as follows: That the bank received the four items of collateral as an unlawful and recoverable preference and treated them as cash and shortly thereafter converted them into cash which was intermingled with the cash of the bank and treated by it as its own; that when the Bank closed it had on hand in cash and cash items, $36,-054.76, which afterwards went into the hands of the Receiver; that the least amount in cash and cash items in the Bank during the period from February 5, 1929, to the close of the business on January 7, 1932, was $30,548.61; that the Bank by collecting bankrupt's notes and bonds and by a sale of his bank stock without the knowledge or consent of the Trustee, held the proceeds of such collections and sale amounting to $8,-870.07, as a Trustee *ex maleficio;* and that said funds were in the possession of the bank when it closed." (R. p. 84).

The Court of Appeals held that the District Court properly found that the Bank held the funds as a Trustee *ex maleficio.* (R. pps. 84, 85). The correctness of this holding is admitted by the petitioner in this Court. (See Summary of Argument, Brief p. 11).

With regard to augmentation and tracing of funds, the Court of Appeals said:

> "We are convinced that the Bank's assets were augmented by, and to the extent of, the proceeds of the collateral, and that those proceeds have in law been traced into the Receiver's hands." (R. p. 87).

It will thus be seen that the findings of fact in both the District Court and the Court of Appeals are the same.

At various places in petitioner's Brief and Petition the three elements necessary to establish his claim, in order to have a preferred claim allowed against an insolvent National Bank, are stated as follows:

> "(1) The relationship is that of Trustee and *cestui que trust;*
>
> "(2) The transaction with the claimant resulted in augmentation or increase of the assets of the insolvent by the property of the claimant or the proceeds thereof in the form of actual cash or other tangible assets;
>
> "(3) That such property or assets of the claimant, or other property identified as being in lieu thereof, can be traced into the hands of the Receiver taking over the assets of the insolvent at the time of suspension." (See Petition and Brief, pps. 7, 11, 12).

A fourth element is also stated by petitioner as follows:

> "(4) That the burden of showing the facts of augmentation and tracing is upon the preferred claimant." (Petition p. 7).

This, however, is not an element of recovery at all, but simply a rule of evidence bearing upon the burden of proof.

Petitioner's counsel admits that when these three elements of recovery are established by a claimant he is entitled to have a priority claim allowed. Aside from the admission, this is undoubtedly the law. See *Schuyler* v. *Littlefield,* 232 U. S. 710; *Connolly* v. *Lang,* 68 Fed. (2d) 199, 201.

In the case of *Page* v. *Arkansas Natural Gas Corporation*, 286 U. S. 269, the first paragraph of the syllabus is as follows:

> "Findings of fact in which both Courts Below concur will not be reviewed by the Supreme Court of the United States."

On this subject the Court, on page 271, said:

> "Many and complicated questions of fact are involved and were argued here, but as they have been found in favor of the respondent by both Courts Below, we do not review them."

See also *U. S. Trustee, et al.* v. *McGowan, et al.* and *U. S.* v. *Bakers Bay Fish Co., et al.*, 290 U. S. 592.

In the instant case the facts having been found by both of the Lower Courts in favor of the respondent, and these facts being admitted by the petitioner to be sufficient to warrant a recovery by the respondent, we take it that this Court will not grant a writ of certiorari.

B. The merits.

On the merits of the case, we refer the Court to the case of *Schumacher* v. *Harriett*, 52 Fed. (2d) 817, the Opinion in the instant case (R. p. 82), and the Answer of the Appellee to the petition for Rehearing in the Court of Appeals. (R. p. 10).

Respectfully submitted,

HARRY C. HEYL,
Peoria, Illinois,
Attorney for Respondent.

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Supreme Court of the United States

OCTOBER TERM, 1934.

No. 374.

Ross C. ADAMS, Receiver of the Farmers National Bank of Pekin, Illinois, *Petitioner,*

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EDWIN V. CHAMPION, Trustee in Bankruptcy of John Fitzgerald, Bankrupt, *Respondent.*

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OCTOBER TERM, 1934.

No. 374.

ROSS C. ADAMS, Receiver of the Farmers National Bank of Pekin, Illinois, *Petitioner*,

vs.

EDWIN V. CHAMPION, Trustee in Bankruptcy of John Fitzgerald, Bankrupt, *Respondent*.

BRIEF OF THE COMPTROLLER OF THE CURRENCY AS AMICUS CURIAE.

Comes now J. F. T. O'Connor, Comptroller of the Currency of the United States, and respectfully submits his brief, as amicus curiae, in support of the petition for writ of certiorari filed by Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, in the above entitled cause.

I.

FOREWORD.

Citation of the opinions below, statement concerning the jurisdiction of the court to issue writ of certiorari, summary

of the facts, specification of errors, and argument of the issues involved, have been fully summarized in the petition and supporting brief filed by the Receiver of the Farmers National Bank of Pekin, Illinois, and therefore reference is here made to the same in the interest of avoiding repetition.

II.

INTEREST OF THE COMPTROLLER OF THE CURRENCY IN THE CASE FROM AN ADMINISTRATIVE STANDPOINT.

The instant case involves the formulation and statement of the principles of law governing the establishment of preferred claims against insolvent national banks in receivership, and substantially the same issues are present as in the companion case of *Jennings, Receiver of National Bank of America, et al., vs. U. S. Fidelity and Guaranty Company, Respondent, No. 338* of the present term, concerning which petition for writ of certiorari has been filed and in support of which the Comptroller of the Currency has filed a brief as amicus curiae.

The interest of the Comptroller of the Currency in this case, as in that case, is to obtain from this Honorable Court an authoritative statement of the law governing the establishment of preferred claims against insolvent national banks in receivership, so as to enable the Comptroller to apply with uniformity in all jurisdictions in national bank receiverships, the correct doctrines concerning the allowance of preferred claims, and to avoid the confusion and conflict now existing which prevent a proper administration of the law in that respect by the Comptroller as a Federal officer. The position of the Comptroller is set forth in more detail on pages 2 and 3 in the brief filed by the Comptroller of the Currency as amicus curiae in said companion case, and reference is here made to the statements therein contained in that connection in order to avoid repetition.

The instant case turns upon the tracing of funds feature. The now closed bank received in trust four items valued at $8,870.07 and disposed of them prior to suspension, receiving in exchange for three items mere transfers of bookkeeping credits already on its books and for the fourth item a check on an outside bank which was ultimately used in payment of the closed bank's indebtedness, except the sum of $643.24 which the bank Receiver admits constitutes a preferred claim which should be paid subject to pro rata distribution with other preferred claims traceable to the fund or res. The record shows that the balance of the respondent's claim cannot be traced to the funds taken over by the bank receiver under the requirements as to preferred claims established by the weight of authority in the Federal Courts. *Larabee Flour Mills v. First National Bank*, 13 Fed. (2nd) 330, 331; certiorari denied 273 U. S. 727; *City of Miami v. First National Bank*, 69 Fed. (2) 346, 349; *Board of Commissioners v. Strawn*, 157 Fed. 49, 54; *Allied Mills v. Horton*, 65 Fed. (2nd) 708; *American Can Co. v. Williams*, 178 Fed. 420. In directing payment of the full sum of $8,870.07 the court below recognized the claimant's burden of tracing the proceeds to the bank Receiver but, contrary to the record facts, adopted the presumption relied upon by the Circuit Court of Appeals Fourth Circuit, in *Schumacher v. Harriett*, 52 Fed. (2nd) 817 (petitioner's brief, page 21), stating that the facts in both cases are quite analogous.

Prior to the decision of the Circuit Court of Appeals, Fourth Circuit, in *Schumacher v. Harriett*, 52 Fed. (2nd) 817, the Circuit Courts of Appeal were in accord on the tracing of funds rule quoted below from the opinion of the Circuit Court of Appeals for the Eighth Circuit in *Empire State Surety Company v. Carroll County*, 194 Fed. 593-604:

> "It is indispensable to the maintenance by a cestui que trust of a claim to preferential payment by a receiver out of the proceeds of the estate of an insolvent

> that clear proof be made that the trust property or its proceeds went into a specific fund or into a specific identified piece of property which came to the hands of the receiver, and then the claim can be sustained to that fund or property only and only to the extent that the trust property or its proceeds went into it. It is not sufficient to prove that the trust property or its proceeds went into the general assets of the insolvent estate and increased the amount of the value thereof which came to the hands of the Receiver."

The Harriett opinion undertook to liberalize this rule but the liberalized rule has been consistently rejected and criticized by other Circuit Courts of Appeal. (Petitioner's brief, page 22.)

The court below holds that funds in the hands of the bank Receiver, belonging to depositors whose equities, we submit, are at least equal to those of the claimant, shall respond in full for the trust claim of $8,870.07 despite record proof that these funds contain the sum of $643.24 only, in so far as concerns identification as the proceeds of the claimant's transaction. As the result of this decision claims of this character wherein the rule of presumption adopted in the Harriett case is applicable have a preferred status against an insolvent National bank located in the Fourth and Seventh Circuits, but have a general claim status only in the other Circuits, contrary, we submit, to the intent of the National Banking Act which contemplates a plan of liquidation that will be uniform throughout the 48 States. *Cook County National Bank v. United States*, 107 U. S. 445, 448; *First National Bank v. Selden*, 120 Fed. 212, 215. The decision in the instant case appears to be in direct conflict with the principles of law heretofore applied in the Circuits other than the Fourth and Seventh Circuits and with the principles applied and stated by this Court in *Schuyler v. Littlefield*, 232 U. S. 707, 713; *Pottorff vs. Texas & Pacific Railroad*, 291 U. S. 245, 261, Note 19; *Blakey v. Brinson*, 286 U. S. 254.

Every effort is being made by the appropriate Federal agencies involved to give speedy relief to the creditors and depositors of insolvent National banks. A decision by this court settling the tracing of funds issues of law involved in the instant case and the companion case of Jennings v. United States Fidelity & Guaranty Company, now pending in this court on petition for writ of certiorari, No. 338 this term,—regardless of whether the decision below be affirmed or reversed,—will be of inestimable aid to the Comptroller in disposing of similar pending claims and will unquestionably substantially expedite the liquidation of National banks in Receivership by making possible the disposition of numerous other suits pending in the Federal Courts, involving the same issues, and by eliminating future litigation of the same type.

III.

CONCLUSION.

The Comptroller of the Currency therefore earnestly urges this Honorable Court to entertain the petition for writ of certiorari filed by the Receiver in the instant case.

Respectfully submitted,

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Comptroller of the Currency.

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SUPREME COURT OF THE UNITED STATES.

No. 374.—October Term, 1934.

Ross C. Adams, Receiver of the Farmers National Bank of Pekin, Illinois, Petitioner,
vs.
Edwin V. Champion, Trustee in Bankruptcy of John Fitzgerald, Bankrupt, Respondent.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.

[February 4, 1935.]

Mr. Justice Cardozo delivered the opinion of the Court.

A trustee in bankruptcy asserts a claim against the receiver of a national bank for the value of property received by the bank as an unlawful preference. The receiver admits the validity of the claim if it is placed upon the same level as the claims of creditors at large. The trustee insists that the claim must have priority on the ground that the avails of the unlawful preference are subject to a trust.

In September, 1928, the bankrupt, John Fitzgerald, had overdrawn his deposit account with the Farmers National Bank of Pekin, Illinois, and was also indebted to the bank upon promissory notes. In response to a demand for collateral security he delivered to the bank notes of other persons, as well as a certificate of stock, the whole of the face or par value of about $35,000. Most of the securities so delivered have been returned to the trustee and are not in controversy now. Four items only are the subject of this suit.

The bank received from Fitzgerald on September 7, 1928, a certificate for ten shares of its own stock, a promissory note of Charles Graff for $3,000, a promissory note of W. C. Sommer for $1,000, and notes or bonds of Veesaert for $5,000, reduced later by $1,597.31 paid upon account. Within a period of four months (on October 26, 1928), creditors of Fitzgerald filed a petition in bankruptcy, an adjudication following in November of that year. No

election was made by the trustee in bankruptcy to reclaim the collateral as an unlawful preference till July 20, 1929, or if there was an earlier election, it is not shown by the record. In the meantime the bank, which continued as a going concern until January, 1932, had disposed of three of the contested items of security as follows: On February 9, 1929, after having credited the bankrupt with a dividend of $30, it sold the ten shares of its own stock to one Cullinan, a depositor. The price was $3,000, by concession the fair value. Payment was effected by charging the deposit account of the purchaser with what was owing for the shares. On April 12, 1929, the bank collected $3,183.78 upon the note of Charles Graff by charging that amount against the deposit balance to his credit. On April 16, 1929, it collected $1,059.98 upon the note of W. C. Sommer by a charge against his balance. Nothing was received upon the Veesaert bonds, the fourth contested item, till December, 1930. The bank then had a payment on account to the extent of $1,597.31, the payment being made by the deposit of a check to its credit in the First National Bank of Chicago, Illinois. The balance in that account was afterwards reduced to $776.57, which latter amount, together with the bonds themselves, the receiver stands ready to transfer to the trustee.

The election by the trustee to reclaim the collateral securities in behalf of the estate was announced, as we have seen, on July 20, 1929, and was manifested by the beginning of a suit for appropriate relief. No charge was made that the transaction was voidable for any actual fraud. The suit was under § 60b of the National Bankruptcy Act (11 U. S. C. § 96) upon the ground that the effect of the transaction was to prefer one creditor over others, and that the creditor, the bank, had reasonable cause to believe that such effect would follow.* Under *Schoenthal* v. *Irving Trust Co.*, 287 U. S. 92, an action at law could have been maintained for the recovery of the property or its value. Without objection, how-

*"If a bankrupt shall . . . have made a transfer of any of his property, and if, at the time of the transfer, . . . and . . . within four months before the filing of the petition in bankruptcy . . . , the bankrupt be insolvent and the . . . transfer then operate as a preference, and the person receiving it or to be benefited thereby, or his agent acting therein, shall then have reasonable cause to believe that the enforcement of such . . . transfer would effect a preference, it shall be voidable by the trustee and he may recover the property or its value from such person. . . ." § 60b; 11 U. S. C. § 96.

ever, the suit was tried in equity. Cf. *Buffum* v. *Peter Barceloux Co.*, 289 U. S. 227, 235. It ended on June 24, 1932, in a decree invalidating the transactions of September 7, 1928, as constituting a forbidden preference, and directing the return of the securities, or the value of such as had been converted into money.

During the years of litigation the bank had suffered reverses, and on January 8, 1932, it was closed by the Comptroller of the Currency. The receiver appointed by the Comptroller was not a party to the suit to invalidate the preference. After the entry of a decree, the trustee in bankruptcy petitioned for an order instructing the receiver that the four contested items were a preferred charge upon the assets, and that payment should be made accordingly. The District Court granted the relief prayed for, and upon appeal to the Court of Appeals for the Seventh Circuit the order was affirmed. 70 F. (2d) 956. A writ of certiorari issued from this court.

If we except a small item conceded by the receiver, we think the reasons are inadequate for the imposition of a trust in the nature of a preference upon the funds of this insolvent bank.

1. For convenience the first of the contested items, the proceeds of the stock certificate, will be considered by itself, the conclusion appropriate for this item being typical of the conclusion appropriate for the others.

The acceptance by the bank of the certificate delivered by Fitzgerald on September 7, 1928, was not a wrongful act whereby the bank forthwith became subject to the duties and liabilities of a trustee *ex maleficio*. One who acquires a security with reasonable cause to believe that the effect will be a preference does not from that alone become a party to a fraud. *Van Iderstine* v. *National Discount Co.*, 227 U. S. 575, 582; *Watson* v. *Adams*, 242 Fed. 441, 444, 445; *Dean* v. *Davis*, 242 U. S. 438, 444; *Keppel* v. *Tiffin Savings Bank*, 197 U. S. 356; *Carson* v. *Federal Reserve Bank*, 254 N. Y. 218, 234. If bankruptcy is averted altogether, or postponed beyond four months, the security will stand, though a preference was intended at the time of its acceptance. So also a change of assets or liabilities before bankruptcy arrives may mean the difference between a preference and a ratable division. *Haas* v. *Sachs*, 68 F. (2d) 623; *Irving Trust Co.* v. *Townsend*, 65 F. (2d) 406, 408; *Mansfield Lumber Co.* v. *Sternberg*, 38 F. (2d) 614, 617; *Rogers* v. *Page*, 140 Fed. 596, 606; *In re Henry C. King Co.*, 113 Fed.

110, 111; *Rubenstein* v. *Lottow,* 223 Mass. 227, 229, *et seq.* The bank took the risk that in future and indeterminate contingencies it might be compelled to return what it accepted or the value. At the outset it was not a trustee *ex maleficio* or otherwise. It was a bailee and nothing more.

If a trust was not created in September, 1928, through the acceptance of a security which has turned out to be a preference, none was in existence on February 9, 1929, when part of that security, the certificate of stock, was delivered to a purchaser. True, by that time the debtor was in bankruptcy, but the other uncertainties, for anything here shown, were as indefinite as ever. The accurate determination of assets and liabilities had still to wait upon the process of proof and liquidation. At most the security was voidable, not void, and the trustee up to that time had made no move to avoid it. A suit would have been a sufficient election, even though not preceded by a demand (*Eau Claire National Bank* v. *Jackman,* 204 U. S. 522, 534, 535; *Stephens* v. *Pittsburg Plate Glass Co.,* 36 F. (2d) 953), but as yet there had been no suit, nor statement that a suit was coming. To turn the bank into a wrongdoer in the absence of actual fraud, to charge it with all the liabilities growing out of a constructive trust, there was need of some act of avoidance that would put the brand of guilt upon it. Cf. *Boyd* v. *Dunlap,* 1 Johns. Ch. 478, 482, per Kent, Ch. We hear of no such act till July, 1929, when the trustee in bankruptcy brought suit to declare the preference a nullity.

The sale of the stock certificate to Cullinan on February 9, 1929, must be approached and considered in the light of the relation then existing. There was then no trust *ex maleficio,* whereby the bank was chargeable as a wrongdoer for parting with the shares. There was no trust implied in fact, unless it be the fiduciary obligation assumed by a bailee to act with prudence and fidelity in the disposition of the pledge. The trustee does not assert that this obligation has been violated. On the contrary he concedes that the price was equal to the value. With its duty thus defined and measured, the bank agreed with Cullinan to accept payment of the price by canceling to an equivalent extent the debt due him as a depositor. Cf. *Jennings* v. *United States Fidelity & Guaranty Co.,* February 4, 1935, — U. S. —; *Old Company's Lehigh, Inc.* v. *Meeker,* February 4, 1935, — U. S. —. We do not need to con-

sider whether effect would be given to such an agreement according to its form if the bank at that time had been under a present duty to set up a trust as to the proceeds to the use of the bankrupt or of the trustee as his successor. For the purposes of this case we assume, though we do not hold, that a trust in that event would attach to the cash assets in the vaults to an equivalent amount. A different result follows when there is neither trust to be set up nor wilful wrong to be repaired. The bank, when it parted with the certificate, had a solvent, going business, and did not make the transfer with any fraudulent or obstructive purpose. There is no reason in such circumstances why the transaction should be treated retrospectively as something other than it was meant to be. *Jennings* v. *United States Fidelity & Guaranty Co., supra.* Equity fashions a trust with flexible adaptation to the call of the occasion.

Other remedies were at hand sufficient for the needs of justice. When the preference was avoided, the bank became chargeable like any common law debtor with a duty of restitution to the extent of the value of the property disposed of. There might even be a duty, if the proceeds were intact, to make return *in specie.* But what is here sought is very different. By a process of analysis a unitary transaction, the cancellation of a debt to a depositor, is treated as if split up into two parts, a fictitious withdrawal by the depositor of coin or other currency, and its return to the bank to be applied upon the purchase. The money so returned is then subjected to a trust and though mingled with other money is viewed as retaining its identity so long as any portion of the fund is discovered to be intact. These fictions and presumptions may serve well enough in their application to one whose act is against equity and conscience at the time of its commission. They may be implements of justice in cases of theft or actual fraud. So, at least, we now assume. In circumstances less flagrant, they will be used more charily. They will not be so applied as to impose a trust by relation upon moneys that have entered into "the stream of the firm's general property" (Holmes, J., in *National City Bank* v. *Hotchkiss,* 231 U. S. 50, 57), and are distinguishable no longer.

For nearly three years after the sale of this stock, the situation stood unchanged. An adequate remedy against the bank through the recovery of an ordinary money judgment belonged to the trustee continuously, and this whether the award of the value

was to be at law or in equity. *Schoenthal* v. *Irving Trust Co., supra; Buffum* v. *Peter Barceloux Co., supra.* There was no attempt during those years to separate the proceeds of the sale from other assets through an injunction or a receivership, nor any hint of a desire to charge a trust upon the proceeds. Not till the suit was at an end and the bank was in the hands of the Comptroller of the Currency did the respondent shift his theory and turn a debt into a trust. By that time new duties had arisen, new interests had intervened. The assets of the bank were now held by the receiver upon a trust for equal distribution. Cf. *Wisdom* v. *Keen,* 69 F. (2d) 349, 350; *Fera* v. *Wickham,* 135 N. Y. 223, 230; *Gerseta Corp.* v. *Equitable Trust Co.,* 241 N. Y. 418, 425. The shift had come too late.

2. What has been said as to the sale of the stock certificate to Cullinan applies with equal force to the second and third of the contested items, the Graff and Sommer notes.

The collections on these notes were made in April, 1929. They were made, not in cash received over the counter, but by cancellation of a debt owing to the makers upon their deposit balance in the bank. There was neither trust, nor claim of trust, until the bank had suspended, and was in the hands of a receiver.

3. The fourth contested item, the collection on the Veesaert bonds, differs from the others in that the payment was received after the trustee in bankruptcy had elected to avoid the preference and had sued for that relief.

The payment was made as we have seen, by the deposit of $1,597.31 in the First National Bank of Chicago, Illinois.

The balance in that account was reduced in 1931 to $776.57. What became of the difference ($820.74) there is nothing to inform us. Evidence is lacking that it was withdrawn in such a form or for such purposes as to be represented by any assets forming part of the estate today. The receiver consents that this item of $776.57, the balance in the Chicago bank, be paid to the respondent as a preferred charge upon the fund.

The decree is reversed and the cause remanded for further proceedings in accordance with this opinion.

It is so ordered.